LEVELING THE INTERNATIONAL PLAYING FIELD WITH THE MARKETPLACE FAIRNESS ACT

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Quill v. North Dakota[2] unbalanced the American retail market with its preference for out-of-state over in-state sellers. The preference under *Quill* is that sellers without *physical presence* in a state cannot be compelled to collect the sales tax. If the buyer does not voluntarily remit the complementary use tax, the purchase is effectively tax-free. As a result, *Quill* is seen as facilitating tax avoidance and driving business to sellers who have no in-state *nexus,* notably e-businesses. Revenue losses are estimated in excess of $10 billion per year.[3]

The reach of the *Quill* decision is international. Preferred sellers can reside just as easily in another country as they can in another State. The international dimension of the *Quill* decision means that legislative efforts to correct *Quill's* preference for out-of-state sellers, like the Marketplace Fairness Act (MFA),[4] also have international implications. This paper provides a rough analytical and quantitative measure of the impact of the MFA on the largest block of foreign businesses selling into the US, businesses selling from the EU.[5]

Analytically, the MFA offers a compliance regime similar to that advanced by the EU Commission for collecting VAT on difficult cross-border transactions. This administrative replication allows outcomes to be compared. Quantitative measures can be extrapolated from trade statistics, and will allow some rough estimate of where the MFA will have its greatest international impact.

Just like the American retail sales tax, the EU VAT has struggled with distance sales. The EU VAT has adopted a solution that is remarkably similar to that found in the MFA. It is a one-stop-shop (OSS) – a single administrative vehicle for multi-jurisdictional compliance. The major difference between the American and European OSSs is that the MFA requires states to certify *private sector* software to perform OSS

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[2] *Quill v. North Dakota*, 504 U.S. 298 (1992) (requiring the *physical presence* of a business within a jurisdiction before a state can require the business to collect a local sales or use tax on local sales).

[3] Donald Bruce, William F. Fox & LeAnn Luna, *State and Local Sales Tax Revenue Losses from E-Commerce*, 52 STATE TAX NOTES 537 (May 18, 2009) (indicating that losses were projected to be $11.4 billion per year by 2012 with a six-year total of $52 billon).

[4] S. 743 (113th) Marketplace Fairness Act of 2013 (also introduced as H.R. 684 and S336).

[5] The transatlantic economy is the largest and wealthiest market in the world, accounting for over 54% of world GDP in terms of value and 40% in terms of purchasing power. *See*: Daniel S. Hamilton & Joseph P. Quinlan, *The Transatlantic Economy 2011 – Annual Survey of Jobs, Trade and Investment between the United States and Europe,* Center for Transatlantic Relations, Johns Hopkins University, Paul H. Nitz School of Advanced International Studies.

functions, whereas the EU requires each Member State to maintain a *government operated* OSS through an Internet portal.

The EU uses its OSS to level the playing field between Community Member States and third countries in a limited market segment – electronically provided services from non-EU suppliers to EU final consumers. It has recently extended its OSS to another limited market segment involving – radio and television broadcasting, telecommunications and electronic services from EU businesses to EU final consumers in other Member States. The MFA is similarly concerned with sales to final consumers, but in the American case the problematical supplies are commonly goods not services. The RST taxes relatively few services.

There are proposals in the EU to extend the OSS throughout the VAT. There are also concerns that (as currently constituted) the EU OSSs over-correct; that is, they provide a *superior* compliance regime for non-EU sellers (in one case), and selective EU suppliers (in another instance), but *deny* the regime to other similarly situated EU sellers. The MFA has the same issue.

This paper is comparative. It considers the OSS solution in the MFA and compares it with the similar OSSs in Articles 359 through 369 of the VAT Directive. Both US and EU systems struggle when their respective destination-based consumption taxes tilt in favor of distant sellers. The playing field is not level – the marketplace is not fair. The MFA takes a slice of the US playing field and levels it. It levels it (a) in States that meet the MFA's conditions – these States are allowed to compel *domestic remote sellers* to collect the retail sales tax. But in the case of (b) States that do not meet the MFA's conditions – the MFA allows *Quill's* dictates to remain in place, and as a result this part of the playing field remains unlevel.

International remote sellers similarly fall into these same two categories, but the ability of a State to compel a foreign remote seller to comply with state tax laws (even after MFA passage) is difficult. This is another slice of the US playing field that remains unbalanced. This aspect of the MFA echoes a problematical area of VAT enforcement. Both the MFA and the EU see the OSS addressing *international remote sellers* through the OSS simplification because the OSS *encourages* remote sellers (who cannot be *forced* to comply) to collect and remit taxes on their remote sales.

If the MFA is enacted, we may find out if the EU's *government-centric* OSS provides more or less *encouragement* than the US's *private sector* OSS. Significant US and EU revenue is at stake. If there is a "better way," it is important to know what it is.

MARKETPLACE FAIRNESS ACT of 2013

On May 6 the Marketplace Fairness Act of 2013 (MFA)[6] passed the US Senate on a vote of 69 to 27. The MFA is one of three "remote seller" bills currently in Congress attempting to correct *Quill.* It is the only one to pass any chamber of Congress. The

[6] S. 743; also S. 336 and H.R. 684.

others are the Main Street Fairness Act (MSFA),[7] and the Marketplace Equity Act (MEA).[8] Each bill builds on the *private sector OSS* in the Streamlined Sales and Use Tax Act (SSUTA).[9] The reason the MFA has drawn the most support is because it is simpler (than the MEA),[10] and because it imposes fewer burdens on the State (than the MSFA).[11]

Each bill overturns *Quill* by conditionally permitting States to require "remote sellers" to collect sales and use tax. The MSFA's condition is SSUTA membership; the MEA's conditions are set out in "minimum simplification requirements" (many of which are drawn from SSUTA);[12] the MFA sets out alternative conditions of either SSUTA membership or adoption of "minimum simplifications" that are similar to those under the MEA. Each of these acts has unique software provisions drawn largely from the SSUTA. They establish *private sector OSSs* with certified software.

SSUTA – voluntary compliance facilitated by an OSS

The genesis of the *private sector OSS* is in the SSUTA. Unable to overturn *Quill,* the states began a project through the National Tax Association in 1997 that led to the adoption of the SSUTA in 2002.[13] SSUTA's approach to *Quill* was to *induce* traders to *voluntarily* collect and remit sales and use taxes that *Quill* held they were not legally obligated to collect.

The inducement was certified software and third party tax collection agents. The agents, certified service providers (CSPs), literally assumed all of the vendor's sales and use tax functions and did so at no cost to the vendor.[14] A variation on the CSP was also advanced. Where certified automated software (CAS) is deployed by the vendor (not a

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[7] S. 1452 and H.R. 2701.

[8] H.R. 3179.

[9] The Streamlined Sales and Use Tax Agreement is available at: http://www.streamlinedsalestax.org/uploads/downloads/Archive/SSUTA/SSUTA%20As%20Amended%205-24-12.pdf. The SSUTA requires its members to harmonize tax base definitions, standardize electronic reporting, move local reporting to the state level, and to streamline audit and collection processes. The SSUTA was adopted on November 12, 2002, and became effective on October 1, 2005. There are twenty-four member states. They are: Arkansas, Georgia, Indiana, Iowa, Kansas, Kentucky, Michigan, Minnesota, Nebraska, Nevada, New Jersey, North Carolina, North Dakota, Ohio, Oklahoma, Rhode Island, South Dakota, Tennessee, Utah, Vermont, Washington, West Virginia, Wisconsin and Wyoming.

[10] For example the MEA does not require a single audit for all jurisdictions in the State (so the audit burden remains high), and the MEA allows three different rates to be used (so the rate simplification is not robust). It also has a lower threshold for exemption ($500,000 of US sales as opposed to $1,000,000 in the MFA, §2(c)), and this will bring more remote sellers into the sweep of the law.

[11] For example, the MSFA mandates SSUTA membership. There have always been difficulties reaching consensus on some issues in the SSUTA and this has kept some of the larger states, like California and New York, out of the agreement. SSUTA membership is only an option under the MFA. Some States may want this option, or may already be a member.

[12] Those standards are: (1) identification of a single revenue authority within the state for the filing of sales and use tax returns; (2) creation of a single sales and use tax return; (3) establishment of a uniform tax base applicable at state and local levels; (4) the provision of adequate software for remote sellers that will substantially reduce the burden on business of collecting tax at multiple rates within the State; and (5) providing relief of liability for any remote seller whose tax determination is in error because of reliance on information provided by the State. MEA, §§ 2(b)(2) and 2(b)(3).

[13] NTA, *Communications and Electronic Commerce Tax Project Final Report* (September 7, 1999).

[14] SSUTA §§ 201, 203, 205.

third-party service provider), and where this software is used properly the vendor is again insulated from liability for errors in determining the proper tax. The SSUTA Governing Board is charged with certifying CSPs and software.[15]

The CSP (and the certified software alone) function as a *private sector OSSs* for the vendor. It determines and reports all sales and use taxes due in all SSUTA member states. What the SSUTA cannot do however is to *compel* the vendor to use the OSS mechanism. *Quill's* physical presence test allows any vendor without presence in a state to refuse to volunteer to collect the tax.

MFA – mandatory compliance facilitated by an OSS

As federal legislation the MFA can do what SSUTA's aggregation of state legislation cannot. The MFA will allow States to exercise jurisdiction over remote sellers making sales into their state.[16] It does so only if the vendor made more than $1 million in remote sales in the US the previous year.[17] The MFA allows states to make compliance mandatory, not voluntary.

If a vendor exceeds the $1 million threshold, then there are two alternate paths that the state can take to bypass the *Quill* mandate. Both involve certified software (certified software providers), and both effectively establish OSSs. The alternatives are:

1. The State is a member of the SSUTA;[18] or
2. The State must "enact [and] ... implement" the minimum simplification requirements, which are:
   - A single state-level agency will administer all State and local sales and use taxes, returns processing, and audits for remote sales.[19]
   - A single audit of a remote seller for all sales and use taxes;[20]
   - A single sales and use tax return will be used for all taxes, and will be filed with the state administrative agency. The return for remote sellers cannot be required to be filed any more frequently than the returns of non-remote sellers.[21]
   - A uniform sales and use tax base for all taxes in the state.[22]
   - Information on taxable products and services, the exemptions, rates, and the boundary database.[23]

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[15] SSUTA § 501.

[16] MFA, §4(5). Remote sales are sales "... into a State, as determined under the sourcing rules under paragraph (7), in which the seller would not legally be required to pay, collect, or remit State or local sales and use taxes unless provided by this Act."
See also SSUTA § 605(A) "... sales into a state in which the seller would not legally be required to collect sales or use tax, but for the ability of that state to require such "remote seller" to collect sales or use tax under federal authority."

[17] MFA,§2(c).

[18] MFA,§2(a).

[19] MFA, §2(b)(2)(A)(i).

[20] MFA, §2(b)(2)(A)(ii).

[21] MFA, §2(b)(2)(A)(iii).

[22] MFA, §2(b)(2)(B).

[23] MFA, §2(b)(2)(D)(i).

- Provision of "software free of charge for remote sellers that calculates sales and use taxes due on each transaction at the time the transaction is completed, that files sales and use tax returns, and that is updated to reflect rate changes … [and] capable of calculating and filing sales and use tax returns in all States qualified under this Act."[24]
- Provision of certification procedures for the software.[25]
- The State will hold the remote seller harmless for errors or omission in the rate information provided by the State,[26] and do the same for certified software providers."[27]
- 30 days notice will be given of any rate changes by any locality in the State.[28]

These options are not identical. The "minimum simplification" option may not only be easier for the States to implement, it may also be more favorable to both merchants and the technology companies (CSPs) who provide the software solutions. The MFA shifts the cost of compliance and the balance of responsibility for software errors from the seller (or the seller's software provider under the SSUTA) to the State.

The MFA is very clear. The minimum simplification alternative is met "only if" the State provides "software free of charge," just as under the SSUTA. In addition, if that software is "provided by certified software providers [it] shall be capable of calculating and filing sales and use tax returns in all States qualified under this Act."[29] This is very clearly the establishment of an OSS – a single compliance portal available free of charge to receive taxes for multiple jurisdictions.

With the MFA there is a substantial compliance-cost reduction for businesses, and substantial risk reduction for businesses and certified software providers. In terms of compliance costs, both tax calculation and return filing functionality are provided free of charge. In terms of compliance risk the MFA shifts these risks back to the State, and does so in a manner that is perfectly in tune with *Quill*.

At its core the Supreme Court's *Quill* decision rests on a perception of unfairness. It is unfair if a State creates an extremely complex retail sales tax regime, and then penalizes businesses if they cannot comply with the law. Under the MFA this will change. If a State wishes to participate in the MFA and require remote sellers to collect the local sales and use tax, and if complexities remain in its sales tax regime that leads to software errors or omissions in tax calculation and reporting, then it is only fair that the State (not the taxpayer or the software provider) be held at fault.

If the MFA becomes law, and if the forty-five states with a sales tax opt either for SSUTA or minimum simplification, then only remote sellers who make less than $1m of

[24] MFA, §2(b)(1)(D)(ii).
[25] MFA, §2(b)(1)(D)(iii)
[26] MFA, §2(b)(1)(E)
[27] MFA, §§2(b)(1)(F) & (G).
[28] MFA, §2(b)(1)(H)
[29] MFA, §2(b)(2)(D).

remote sales in the US will be protected by *Quill*. This will leave *international remote sellers* as the major enforcement area for the States.

With respect to these remote sellers the US States will be in exactly the same position as the EU Member States when they try to collect VAT on electronically provided services from non-EU suppliers to EU final consumers. Collection and remission of the RST will technically be required under the MFA, but enforcement of this obligation will be nearly impossible. The US States and the EU Member States will be in exactly the same position. Compliance will depend on *moral authority* and the *persuasive power* of the OSS.

OSSs IN THE EU

There are two OSSs in the EU, and an active proposal to open up the OSS procedure to all taxpayers. Only the two limited OSSs have been adopted. In both of the adopted OSSs the goal has been to level the playing field for a defined slice of the marketplace.

EU – a limited OSS only for non-EU businesses (B2C)

In the late 1990's the EU became concerned with the large volume of digital products sold to EU customers by non-EU businesses. The issue was sourcing. The *Sixth Directive*[30] sourced these supplies outside the EU, making them not subject to VAT. However, consumption (use and enjoyment) was occurring within the EU.[31] EU sellers of the same services were at a considerable disadvantage with VAT rates ranging from 15% (Luxembourg) to 25% (Denmark).

The playing field was not level. Because the marketplace was tilted in favor of the non-EU seller, sourcing rules were changed and an OSS adopted.

Sourcing rules. Electronically supplied services from non-EU businesses were added to the list of exceptions in the earlier version of Article 56, and a special rule dealing with similar B2C transactions was added to the earlier version of Article 57(1). Tax now became due in the EU because the place of supply was within the EU.

Working out the practical aspects of this change was more complicated. Business-to-business (B2B) transactions from non-EU suppliers, by far the largest part of e-commerce in monetary terms, were handled through a reverse charge procedure. Business-to-consumer (B2C) transactions were more difficult. Consumers do not file

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[30] The SIXTH COUNCIL DIRECTIVE of 17 May 1977 on the harmonization of the laws of the Member States relating to turnover tax – Common system of value added tax: uniform basis of assessment (77/388/EEC) 1977 O.J. (L 145) 1 was repealed and replaced on November 28, 2006 with the RECAST VAT DIRECTIVE. Council Directive 2006/112/EC on the Common system of value added tax, O.J. (L 347) 1. Citations throughout this document will be to both versions. The most updated version will be referenced as the VAT DIRECTIVE.

[31] Specifically, the sourcing issue was that the fall back rule of Article 9(1) [VAT DIRECTIVE, Article 43]. This rule provided that any service not covered in the series of exceptions that make up the rest of the former Article 9 were to be taxed where the supplier was located. In the case of digital services this was frequently outside the EU, and commonly in the US.

VAT returns, thus a reverse charge was not possible. Non-EU businesses were simply required to collect and remit the VAT. However, there was no way to enforce this requirement.

At this juncture, the EU VAT and the RST under the MFA are in exactly the same position. Both *require* overseas businesses to collect and remit a destination-based consumption tax, but neither can *enforce* the requirement.[32] The EU sought to *induce* compliance with its first OSS.

The one-stop-shop (OSS). Articles 359 through 369 (formerly Article 26c) were adopted. Together they provide for an OSS that allows non-EU established businesses to select a single "Member State of identification" where they will register (but are not considered established). VAT from sales made throughout the EU is charged on a destination-basis, and the full sum is paid over to the Member State of identification on a single electronic return. The member state of identification then redistributes the VAT to the appropriate jurisdictions. Everything is required to be digital.

Although the compliance costs and risk of errors are born by the business, filing and payment is streamlined through a dedicated web portal established by the Member State.

EU – a second limited OSS only for EU radio and television broadcasting, telecommunications and electronic services businesses (B2C)

In 2008 the place of supply for services was changed generally from the seller's to the buyer's location. For radio and television broadcasting, telecommunications and electronic services, this was a very significant change. Under the previous sourcing rules it had been common for EU broadcasters to establish themselves in a low tax jurisdiction (Luxembourg was favored at 15%) when broadcasting into high tax jurisdictions (Denmark's 25% rate was avoided).[33]

This sourcing adjustment was so difficult for this industry segment that an agreement to make overall changes could not be reached without selectively delaying the effective date for this industry until January 1, 2015, and then further allowing use of the OSS procedure by these firms.[34]

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[32] If a business was willing to comply with the requirement to collect the VAT on B2C sales, there were essentially two options: they could either (1) establish themselves in a Member State, or (2) register in each Member State where they made taxable supplies. Neither choice was optimal. Although under the first option all digital sales would be sourced to the one EU jurisdiction where the business was established, the establishment process itself led to direct tax obligations. The formerly non-EU business would become a real EU business for tax and regulatory purposes. The second option also had disadvantages. Under this option a business could conceivably be required to register in what was then 25 Member States (now 27), file 25 sets of VAT returns, and do so in as many as 20 different languages. Sourcing of sales under this option would be destination-based.

[33] Council Directive 2008/8/EC of 12 February 2008 amending Directive 2006/112/EC as regards the place of supply of services, O.J. (L 144) 1 (February 20, 2008).

[34] Commission implementing Regulation (EU) No. 815/2012 of 13 September 2012 laying down detailed rules for the application of Council Regulation (EU) No 904/2010 as regards special schemes for non-established taxable persons supplying telecommunications, broadcasting or electronic services to non-

The implementing regulation now distinguishes between two OSSs: (1) the new "Union Scheme" (the special scheme for taxable persons that are established within the Community, but not established within the Member State where the services are supplied) and (2) the older "Non-Union Scheme" (for taxable persons not established within the Community). The regulation structures the OSS process as follows:[35]

- Statement – the taxable person must submit a statement to the Member State where he would like to be *identified* (the Member State of Identification);[36]
    - The Member State cannot refuse the request.
- Updates – the statement must be updated to reflect commencement and cessation of activity;[37]
- Details – the statement must indicate:[38]
    - Name
    - Postal address
    - Electronic address & web site
    - National tax number (if any);
- In the case of a non-EU business a statement that the person is not identified for VAT purposes within the EU.[39]
- Return – a single return is required each quarter which must show:[40]
    - VAT identification number;
    - Total value of supplies made in each Member State;
    - Total amount of VAT due in each Member State;
    - The applicable VAT rate in each Member State.
- Euros – the VAT return must be in euros (unless the Member State of Identification has not adopted the euro).[41]
- Payment – one payment will be made into the bank account designated by the Member State of Identification.[42]
- Record keeping – records must be kept for 10 years.[43]

The VAT paid to the Member State of Identification is reallocated to the appropriate Member State of Consumption. The taxpayer's calculation and allocation is followed. There is no unitary audit, each Member State will audit on its own.

TWO LESSONS FROM THE COMPARTIVE STUDY:

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taxable persons. On October 9, 2012 the Council adopted Regulation (EU) No 967/2012 amending implementing Regulation (EU) No 282/2011 as regards the special scheme for non-established taxable persons supplying telecommunications services, broadcasting services or electronic services to non-taxable persons.

[35] All taxpayer/government communications are required to be electronic.

[36] VAT DIRECTIVE, Articles 359 & 369b.

[37] VAT DIRECTIVE, Article 360 & 369c.

[38] VAT DIRECTIVE, Article 361 & 369e.

[39] VAT DIRECTIVE, Article 364.

[40] VAT DIRECTIVE, Article 365 & 369f.

[41] VAT DIRECTIVE, Article 366 & 369h.

[42] VAT DIRECTIVE, Article 367 &369i.

[43] VAT DIRECTIVE, Article 369 & 369k.

(1) The Over-correction (or under-inclusiveness) Problem of the OSS
(2) Don't forget the International Slice of the Marketplace

There are two lessons to be learned from a comparison of the OSSs in the MFA and the EU VAT. The first has to do with the domestic dynamic that arises when an OSS is implemented and is found to be successful. Businesses that were excluded from the OSS in the beginning seek admission later to capture efficiencies and reduce compliance risks.

Secondly, because the entire area of remote sellers and destination consumption taxes has a strong international component, the quest to level the domestic playing field eventually leads overseas. States should anticipate that foreign cooperation would be forthcoming, and may want to prepare the way for further federal involvement in the US sales tax. The first step in this analysis is to measure the potential revenue flows.

LESSON (1):
The Over-correction (or under-inclusiveness) Problem of the OSS

The EU's OSSs are not open to all taxpayers. Only non-EU businesses selling to EU final consumers, or EU radio and television broadcasting, telecommunications and electronic service firms can use it. However, the efficiency of filing a single pan-EU return through a single web portal has not gone unnoticed by similarly situated businesses established in the EU.

The same situation will (most likely) arise under the MFA. Neither the SSUTA's nor the MFA's OSSs are open to all taxpayers. If the MFA's OSS is a success, it would be reasonable to expect a dynamic similar to that found in the EU to arise in the US.

In March 2004 the EU Commission suggested in a *Consultation Paper* that any EU businesses making supplies (digital or otherwise) directly to EU end users in a Member State other than the state where they were established should be allowed to file under an OSS procedure.[44]

The business response to the *Consultation Paper* was overwhelmingly positive.[45] European businesses urged the expansion of the OSS system. Intra-community B2C, domestic B2C, and even B2B transactions should be allowed to use the OSS, they said. The OSS was seen as a simplification that worked, but had been unfairly open only to foreigners (it was later opened to EU radio and television broadcasting,

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[44] Although not clearly stated in the *Consultation Paper* it appears that non-EU established persons would have to become established to participate. European Commission, *Consultation Paper: Simplifying VAT Obligations, The One-Stop System* (March, 2004) TAXUD/590/2004-EN, page 3.

[45] See for example the response of Eurochambres, *Position Paper 2004: Simplifying VAT Obligations: the One-Stop System.* Eurochambres is a 17 million-member business organization that is the sole European body serving the interests of every sector and every size of European business. Available at: http://www.eurochambres.be/PDF/pdf_position_2004/VAT%20One-Stop-Shop.pdf

telecommunications and electronic service providers). Nevertheless, for political reasons, the proposal in the *Consultation Paper* was not adopted.[46]

The EU Commission's short hand expression for the current situation is that there is a *mini-one-stop-shop.* This expression leaves open an expectation that a comprehensive OSS could be right around the corner. In fact, the Commission proposes that after 2015 there should be a "... managed broadening of the One Stop Shop over time. [But that] ... it's a good idea to wait to see the success of the mini One Stop Shop before embarking on an expansion; and this we will do."[47]

Provided that the MFA passes and the States comply with its conditions, and if they then demand that remote sellers collect the sales and use tax, it may only be a matter of time before in-state businesses request an extension of the MFA's OSS to all taxpayers (whether or not they are making remote sales). The argument will be: Why should an out-of-state seller be provided tax software free of charge, and be held harmless for errors when in-state sellers are not accorded the same benefits?

This is a difficult argument to rebut in the context of a tax reform that is based on fairness. Thus, apart from aiming to level the playing field between e-commerce and brick-and-mortar businesses, as a side-effect, the MFA could facilitate tax collection and compliance in the whole economy: Although the bill's, measures target specific companies, they could potentially benefit all.

LESSON (2):

Don't forget the International Slice of the Marketplace

In terms of US imports, the second largest piece of the American cross-border trade is European. In 2011, trade with the EU27 accounted for 16.9% of the total value of US imports, exceeded only by China at 18.8%.[48] In order to arrive at an estimate of the volume of international trade likely to be affected by the MFA (remote sales by

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[46] The main reason this expanded OSS was not adopted had to do with the clearinghouse mechanism that would need to be established. In the Commission's mind the main problem was a matter of trust. Algirdas Semeta, the European Commissioner for Taxation, Customs, Anti-fraud and Audit indicated:

> The One Stop Shop has many merits. It can bring substantial simplification and cost reductions for businesses and member states. But for it to work in practice, *member states must trust each other* to collect the VAT on their behalf. It needs to be asked whether that degree of confidence between the member states currently exists.

Algirdas Semeta, *The mini-One Stop Shop for VAT – the start of something big!* WORLD COMMERCE REVIEW (June 2012) 29 (emphasis added). See also: Sijbren Cnossen, (Commentary on Ian Crawford, Michael Keen & Stephen Smith, *Value Added Tax and Excises*, Ch 4 in Institute for Fiscal Studies, DIMENSIONS OF TAX DESIGN: THE MIRRLEES REVIEW) at subheading *Exporter Rating System Proposed by the European Commission* at 377-382 *available at*: http://www.ifs.org.uk/mirrleesreview/dimensions/ch4.pdf (discussing the political discord arising with the proposal of a clearing house).

[47] Algirdas Semeta, *supra* note **Error! Bookmark not defined.**9, at 29.

[48] *United States: EU Bilateral Trade and Trade with the World* (May, 2013) European Commission. Available at: http://trade.ec.europa.eu/doclib/docs/2006/september/tradoc_113465.pdf

businesses that exceed the MFA's $1,000,000 threshold) we need to start with aggregate EU-US trade data.[49]

Table 1 shows the number of European enterprises exporting to the US in 2010, with the exception of Belgian and Irish data (this data is not available in the OECD Trading Partners Database). The upper estimate of the number of EU firms that could potentially be required to charge sales tax under the MFA is, therefore, approximately 146,000. These firms generated $253 billion of EU-US trade value in 2010.

Under *Quill* most of these firms would never have had an obligation to collect sales or use tax. The vast majority of these firms have *no physical presence* in the US. In 2009, 16 EU Member States with 141,331 US-exporting businesses reported only 15,920 US based affiliates.

There are several reasons why not all 146,000 EU exporters will want to access the *private sector OSS* of the MFA.

First, some firms' remote sales will not surpass $1 million. The majority of these will likely be micro-enterprises, usually defined as enterprises with fewer than 10 employees and turnover below EUR 2 million. While we cannot control for turnover, OECD Trade by Size Classes Database, Rev.4 provides information on the size class of all European firms involved in external EU-trade. By identifying the fraction of micro-enterprises in the total population of exporting firms we can get a rough idea of their number in the subsample of EU-US exporters (only).

Thus, we find that 44% of all EU companies trading with partners outside the EU have between 1 and 9 employees. Assuming that the percent of micro-enterprises is similar for the sample of US-exporting firms, then roughly 64,800 of these firms are likely to be too small to exceed the $1 million small seller threshold.[50]

Even though almost half of all firms involved in external EU-trade are micro-enterprises, they account for only 8% of the value of external trade. In contrast, 3% of companies with more than 250 employees generate 53% of the value of external EU trade. These larger firms and SMEs, or roughly 80,000 firms are in all likelihood above the MFA threshold. Yet, for reasons explained below, this does not mean that they will

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[49] It is important to note that the MFA states that, "... the remote sales of 2 or more persons shall be aggregated if:

1. such persons are related to the remote seller within the meaning of subsections (b) and (c) of section 267 or section 707(b)(1) of the Internal Revenue Code of 1986; or
2. such persons have 1 or more ownership relationships and such relationships were designed with a principal purpose of avoiding the application of these rules."

MFA, §2(c) (1) & (2).

These conditions eliminate incentives for the establishment of multiple sister companies without physical presence by the parent or other subsidiaries, whose goal would be to maintain sales below the threshold and thus, avoid the collection of sales tax.

[50] This assumption is rather strong as it is possible that micro-enterprises are mostly trading with partners in close geographical proximity to the EU, whereas big exporters are engaged in overseas trade.

all be subject to state efforts to compel sales and use tax collection as a remote seller under the MFA. Nor does it mean that the sales and use tax on US imported products is fully lost.

Second, many SMEs and large corporations active in the US market already use the services of giant resellers like Digital River ($22 billion revenue) for the sale of their digital products. In fact, such resellers typically provide comprehensive services – they are a payment platform, offering both digital and physical product fulfillment as well as marketing of the product. What this means is that the obligation to collect the sales tax will not rest with the remote foreign seller but with the American reseller. The burden of compliance would be shifted from the international party onto the domestic player in the American market. Some of the sales and use tax would already have been captured in states in which a reseller is physically located.

Third, on B2B sales the American buyer will most likely remit the use tax, but on B2C sales the tax is most likely not reported. This is the same pattern that plays out in the EU where the reverse charge collects the VAT on B2B cross-border transactions, but there is low compliance in a comparable B2C transaction.

It is useful therefore, to look at the composition of European imports into the US. The OECD Statistics on Measuring Globalization contain a dataset on bilateral trade in intermediate goods and services with the latest recorded year being 2005 (Table 1, Column 5). In 2005, European exports of intermediate goods/services to the US were $198 billion or 63% of the value of total exports to the US in 2006.[51] As mentioned above, a large portion of the use tax on these B2B sales may already be collected. Nevertheless, the remaining 37% of trade value is likely generated by B2C transactions, which implies significant foregone sales tax revenue.

Apart from intermediate goods, we can disaggregate EU exports to the US by sector, the most interesting being wholesale, retail trade and repair (Table 1, Columns (2) and (4)). In 2010, 30% of all European exporters conducted wholesale and/or retail trade with the US amounting to $27 billion, or 10% of total value.

To summarize, *Quill* is not dead. Currently, international traders without a physical presence in the US have no obligation to collect the sales and use tax barring:

(a) passage of the MFA (or another similar federal statute),

(b) state membership in SSUTA or satisfaction of "minimum simplifications" requirements, and

[51] The earliest available year with data for the value of European exports to the US is 2006 in OECD Trading Partners, Rev. 3. The calculation of the percent excludes data for Bulgaria, Germany, Greece, Malta, the Netherlands, Spain and the UK, all of which have missing observations for the value of trade with the US for 2006.

(c) a State statute requiring remote sellers to collect the sales and use tax on in-state sales.

Table 1 Number of EU Enterprises Exporting to the US and Value of Exports, 2010

Country	(1) Total number of enterprises exporting to the US	(2) Wholesale, retail trade and repair, number of enterprises	(3) Value of trade in mil USD (total number of enterprises)	(4) Value of trade in mil USD (wholesale, retail trade and repair	(5) Value of intermediate goods and services, mil USD, 2005
Austria	2,694	893	6,225.79	631.063	4,074.169
Bulgaria	725	197	277.733	41.149	228.8975
Cyprus	143	51	15.733	1.66	305.0888
Czech Republic	2,166	578	1,813.47	201.9	1,689.441
Denmark	3,175	1,213	5,944.5	1208.34	4,963.871
Estonia	251	54	431.341	7.475	198.8327
Finland	1,758	427	4,633.74	63.611	2,367.472
France	19,251	6,478	28,533	4398.48	20,037.14
Germany	20,795	5,705	77,481.1	3085.18	45,526.91
Greece	2,422	770	1,533.11	78.682	5,155.519
Hungary	1,243	328	1,986.17	651.78	1,380.397
Italy	29,129	7,075	25,457.3	2473.95	18,274.61
Latvia	274	70	120.671	13.079	177.363
Lithuania	384	106	558.691	19.153	196.442
Luxembourg	157	82	376.932	11.3	631.1612
Malta	147	37	258.335	23.483	246.5662
Netherlands	5,617	2,101	18,523.5	5640.39	8,649.117
Poland	3,625	911	2,549.36	292.132	1,548.474
Portugal	2,236	544	1,723.08	94.134	1,534.645
Romania	792	155	652.963	17.317	943.69
Slovakia	481	98	899.616	11.849	334.3952
Slovenia	493	86	360.418	6.669	229.232
Spain	11,360	3,393	8,269.75	1301.47	7,666.638
Sweden	6,351	2,126	11,268.9	471.939	7,825.544
United Kingdom	29,554	10,217	53,417	6,337.45	40,226.83
Total	145,178	43,695	253,312.2	27,083.64	198,177.5

Source: OECD Trading Partners Database, Rev.4; OECD Bilateral Trade in Intermediate Goods and Services

If the MFA becomes law, and if the use tax on imported intermediate and B2C goods is partially collected, it is reasonable to assume that the international slice of US trade will contribute significantly to rising sales tax revenue. It is, however likely, that many international firms would outsource the service of sales tax collection to US resellers, so the obligation to comply with state tax laws may ultimately reside with US businesses. Nevertheless, if approximately 80,000 EU businesses exceed the $1 million remote sale threshold, and if these firms are making more than $200 billion in US sales, it is likely that a significant amount of recovered sales and use tax revenue will come from the international slice of the unbalanced American marketplace.

CONCLUSION

The EU and the US Sates are looking at much the same problem when they endeavor to have remote sellers collect and remit destination-based consumption taxes. Both systems recognize that simply having a law in place requiring collection is not sufficient. Both systems have adopted OSSs and compliance simplifications to induce or persuade remote sellers to comply. The EU's preference for a *government-centric OSS* and the US preference for OSSs that involve *third-parties and certified software* may have very different success profiles. This is an important assessment that is yet to come, but it suggests that the US may want to borrow a solution from the EU, or the EU may want to borrow a solution from the US States. Both sides need to be open to the possibility.

At the present time, it is clear that there is room for considerable international cooperation. Algirdas Semeta, the European Commissioner for taxation indicated that the EU Commission is anxious to cooperate. He observes:

> There is no effective way of ensuring compliance if a business located in California, for example, provides e-services to a private individual in Slovakia and does not register for the e-commerce scheme and pay Slovak VAT what can the national tax authorities do realistically? *The Commission is addressing this issue and has asked member states for a mandate to negotiate with third countries on this issue from a collective position of power.* For the time being, though, compliance depends on the willingness of suppliers in third countries to assume their legal obligations.[52]

If the EU is concerned about a remote seller in California making sales into Slovakia, then the California Board of Equalization is most likely equally concerned about a remote seller in France making sales into Los Angles.

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[52] Algirdas Semeta, *The mini-One Stop Shop for VAT – the start of something big!* WORLD COMMERCE REVIEW (June 2012) 28 (emphasis added).

Cooperation could be government-to-government, but it could also be through software certification. If the EU adopted the March 2004 *Consultation Paper* proposal and moved generally to OSS compliance, and if the EU decided to adopt the *private sector* software model advanced by SSUTA and the MFA, then it would be a relatively easy matter to jointly certify global software platforms that would comply with all US and EU transaction taxes.

There are already a number of certified software packages in the US that are fully compliant with the thousands of US RST jurisdictions. Some of these packages are also fully compliant with the EU VAT. Joint EU-SSUTA certification may be just ahead if the MFA proves to be a success at persuading remote sellers to comply with collection obligations. It would certainly be a software solution that would be in high commercial demand for the businesses engaged in transatlantic trade – the largest and wealthiest market in the world that accounts for over 54% of world GDP in terms of value and 40% in terms of purchasing power.

FEATURED PERSPECTIVES

The International Implications of the U.S. Marketplace Fairness Act for E-Commerce

by Richard T. Ainsworth and Boryana Madzharova

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Quill v. North Dakota[1] unbalanced the U.S. retail market with its preference for out-of-state over in-state sellers. The preference under *Quill* is that sellers without physical presence in a state cannot be compelled to collect the sales tax. If the buyer does not voluntarily remit the complementary use tax, the purchase is effectively tax free. As a result, *Quill* is seen as facilitating tax avoidance and driving business to sellers that have no in-state nexus, notably e-businesses. Revenue losses are estimated to be in excess of $10 billion per year.[2]

The reach of the *Quill* decision is international. Preferred sellers can reside just as easily in another country as they can in another state. The international dimension of the *Quill* decision means that legislative efforts to correct *Quill*'s preference for out-of-state sellers, like the Marketplace Fairness Act of 2013 (MFA),[3] also have international implications. This article provides a rough analytical and quantitative measure of the effect of the MFA on the largest block of foreign businesses selling into the U.S.: businesses selling from the EU.[4]

The MFA offers a compliance regime similar to that advanced by the European Commission for collecting VAT on difficult cross-border transactions. This administrative replication allows outcomes to be compared. Quantitative measures can be extrapolated from trade statistics and will allow a rough estimate of where the MFA will have its greatest international impact.

Just like the U.S. retail sales tax, the EU VAT has struggled with distance sales. The EU VAT regime has adopted a solution that is remarkably similar to that found in the MFA. It is a one-stop shop (OSS) — a single administrative vehicle for multijurisdictional compliance. The major difference between the U.S. and European OSSs is that the MFA requires states to certify private sector software to perform OSS functions,

[1] *Quill v. North Dakota*, 504 U.S. 298 (1992) (requiring the physical presence of a business within a jurisdiction before a state can require the business to collect a local sales or use tax on local sales).

[2] Donald Bruce, William F. Fox, and LeAnn Luna, "State and Local Sales Tax Revenue Losses From E-Commerce," *State Tax Notes*, May 18, 2009, p. 537 (indicating that losses were projected to be $11.4 billion per year by 2012, with a six-year total of $52 billon).

[3] S. 743 (113th Congress), also introduced as H.R. 684 and S. 336.

[4] The transatlantic economy is the largest and wealthiest market in the world, accounting for over 54 percent of world GDP in terms of value and 40 percent in terms of purchasing power. *See* Daniel S. Hamilton and Joseph P. Quinlan, "The Transatlantic Economy 2011 — Annual Survey of Jobs, Trade and Investment Between the United States and Europe," Center for Transatlantic Relations, Johns Hopkins University, Paul H. Nitze School of Advanced International Studies.

whereas the EU requires each member state to maintain a government-operated OSS through an Internet portal.

The EU uses its OSS to level the playing field between member states and third countries in a limited market segment: electronically provided services from non-EU suppliers to EU final consumers. It has recently extended its OSS to another limited market segment involving radio and television broadcasting; telecommunications; and electronic services from EU businesses to EU final consumers in other member states. The MFA is similarly concerned with sales to final consumers, but in the U.S. the problematical supplies are commonly goods, not services. The retail sales tax (RST) taxes relatively few services.

There are proposals in the EU to extend the OSS throughout the VAT regime. There are also concerns that (as currently constituted) the EU OSSs overcorrect — that is, they provide a superior compliance regime for non-EU sellers (in one case), and selected EU suppliers (in another instance), but deny the regime to other similarly situated EU sellers. The MFA has the same issue.

This article is comparative. It considers the OSS solution in the MFA and compares it with the similar OSSs in articles 359 through 369 of the VAT directive. Both the U.S. system and EU system struggle when their respective destination-based consumption taxes tilt in favor of distant sellers. The playing field is not level — the marketplace is not fair. The MFA takes a slice of the U.S. playing field and levels it — in states that meet the MFA's conditions. These states are allowed to compel domestic remote sellers to collect the retail sales tax. But the MFA allows *Quill*'s dictates to remain in place for states that don't meet the MFA's conditions, and as a result, this part of the playing field remains unlevel.

International remote sellers similarly fall into these same two categories, but the ability of a state to compel a foreign remote seller to comply with state tax laws (even after MFA passage) is difficult. That is another slice of the U.S. playing field that remains unbalanced. This aspect of the MFA echoes a problematical area of VAT enforcement. Both the MFA and the EU see the OSS as addressing international remote sellers through its simplification, because the OSS encourages remote sellers (which cannot be forced to comply) to collect and remit taxes on their remote sales.

If the MFA is enacted, we may find out if the EU's government-centric OSS provides more or less encouragement than the U.S.'s private sector OSS. Significant amounts of U.S. and EU revenue are at stake. If there is a better way, it is important to know what it is.

I. Marketplace Fairness Act

On May 6 the U.S. Senate passed the MFA on a vote of 69 to 27. The MFA is one of three remote seller bills currently in Congress attempting to correct *Quill*. It is the only one to pass any chamber of Congress. The others are the Main Street Fairness Act (MSFA)[5] and the Marketplace Equity Act (MEA).[6] Each bill builds on the private sector OSS in the Streamlined Sales and Use Tax Agreement.[7] The reason the MFA has drawn the most support is because it is simpler (than the MEA)[8] and imposes fewer burdens on the state (than the MSFA).[9]

Each bill overturns *Quill* by conditionally permitting states to require remote sellers to collect sales and use tax. The MSFA's condition is SSUTA membership; the MEA's conditions are set out under "minimum simplification requirements" (many of which are drawn from the SSUTA)[10]; and the MFA sets out alternative conditions of either SSUTA membership or adoption of minimum simplifications that are similar to those under the MEA. Each of these acts has unique software provisions drawn largely from the SSUTA. They establish private sector OSSs with certified software.

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[5]S. 1452 and H.R. 2701.

[6]H.R. 3179.

[7]*Available at* http://www.streamlinedsalestax.org/uploads/downloads/Archive/SSUTA/SSUTA%20As%20Amended%205-24-12.pdf. The SSUTA requires its members to harmonize tax base definitions; standardize electronic reporting; move local reporting to the state level; and streamline audit and collection processes. The SSUTA was adopted on November 12, 2002, and became effective on October 1, 2005. The 24 member states are Arkansas, Georgia, Indiana, Iowa, Kansas, Kentucky, Michigan, Minnesota, Nebraska, Nevada, New Jersey, North Carolina, North Dakota, Ohio, Oklahoma, Rhode Island, South Dakota, Tennessee, Utah, Vermont, Washington, West Virginia, Wisconsin, and Wyoming.

[8]For example, the MEA does not require a unitary audit for all jurisdictions in the state (so the audit burden remains high), and it allows three different rates to be used (so the rate simplification isn't robust). It also has a lower threshold for exemption ($500,000 of U.S. sales as opposed to $1 million in the MFA, section 2(c)), which will bring more remote sellers under the law.

[9]For example, the MSFA mandates SSUTA membership. There have always been difficulties reaching consensus on some issues in the SSUTA, which has kept some of the larger states, like California and New York, out of the agreement. SSUTA membership is only an option under the MFA. Some states may want this option or may already be a member.

[10]Those requirements are:

(1) identification of a single revenue authority within the state for the filing of sales and use tax returns;

(2) creation of a single sales and use tax return;

(3) establishment of a uniform tax base applicable at the state and local levels;

(4) the provision of adequate software for remote sellers that will substantially reduce the burden on businesses of collecting tax at multiple rates within the state; and

(5) providing relief of liability for any remote seller whose tax determination is erroneous because of reliance on information provided by the state.

MEA sections 2(b)(2) and 2(b)(3).

A. SSUTA — Voluntary Compliance

The genesis of the private sector OSS is in the SSUTA. Unable to overturn *Quill,* the states began a project through the National Tax Association in 1997 that led to the adoption of the SSUTA in 2002.[11] The SSUTA's approach to *Quill* was to encourage traders to voluntarily collect and remit sales and use taxes that *Quill* held they weren't legally obligated to collect.

The incentives for traders were certified software and third-party tax collection agents. The agents, certified service providers (CSPs), assumed all of the vendor's sales and use tax functions and did so at no cost to the vendor.[12] A variation on the CSP was also advanced. When certified automated software is used by the vendor (not a third-party service provider), and when this software is used properly, the vendor is again insulated from liability for errors in determining the proper tax. The SSUTA governing board is charged with certifying CSPs and software.[13]

The CSP (and the certified software, alone) function as a private sector OSS for the vendor. It determines and reports all sales and use taxes due in all SSUTA member states. What the SSUTA cannot do, however, is compel the vendor to use the OSS mechanism. *Quill*'s physical presence test allows any vendor without presence in a state to refuse to volunteer to collect the tax.

B. MFA — Mandatory Compliance

As federal legislation, the MFA can do what SSUTA's aggregation of state legislation cannot. The MFA will allow states jurisdiction over remote sellers making sales into the state.[14] It does so only if the vendor made more than $1 million in remote sales in the U.S. the previous year.[15] The MFA allows states to make compliance mandatory.

If a vendor exceeds the $1 million threshold, then there are two alternate paths that the state can take to bypass the *Quill* mandate. Both involve certified software, and both effectively establish OSSs. The alternatives are:

- the state is a member of the SSUTA[16]; or
- the state must enact and implement the minimum simplification requirements, which are:
  - — A single state-level agency will administer all state and local sales and use taxes, return processing, and audits for remote sales.[17]
  - — A single audit of a remote seller for all sales and use taxes.[18]
  - — A single sales and use tax return will be used for all taxes and filed with the state administrative agency. The returns for remote sellers cannot be required to be filed any more frequently than the returns of non-remote sellers.[19]
  - — A uniform sales and use tax base for all taxes in the state.[20]
  - — Information on taxable products and services, exemptions, rates, and the boundary database.[21]
  - — The provision of "software free of charge for remote sellers that calculates sales and use taxes due on each transaction at the time the transaction is completed, that files sales and use tax returns, and that is updated to reflect rate changes . . . [and] capable of calculating and filing sales and use tax returns in all states qualified under this Act."[22]
  - — The provision of certification procedures for the software.[23]
  - — The state will hold the remote seller harmless for errors or omissions in the rate information provided by the state[24] and do the same for CSPs.[25]
  - — Thirty days notice will be given of any rate changes by any locality in the state.[26]

These options aren't identical. The minimum simplification option may be not only easier for the states to implement, but also more favorable to both merchants and the technology companies (the CSPs) that provide the software solutions. The MFA shifts the cost of compliance and the balance of responsibility for software errors from the seller (or the seller's software provider under the SSUTA) to the state.

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[11]NTA, "Communications and Electronic Commerce Tax Project Final Report" (Sept. 7, 1999).

[12]SSUTA sections 201, 203, and 205.

[13]SSUTA section 501.

[14]MFA section 4(5). Remote sales are sales "into a State, as determined under the sourcing rules under para. (7), in which the seller would not legally be required to pay, collect, or remit State or local sales and use taxes unless provided by this Act."

See also SSUTA section 605(A): "Sales into a state in which the seller would not legally be required to collect sales or use tax, but for the ability of that state to require such 'remote seller' to collect sales or use tax under federal authority."

[15]MFA section 2(c).

[16]MFA section 2(a).

[17]MFA section 2(b)(2)(A)(i).

[18]MFA section 2(b)(2)(A)(ii).

[19]MFA section 2(b)(2)(A)(iii).

[20]MFA section 2(b)(2)(B).

[21]MFA section 2(b)(2)(D)(i).

[22]MFA section 2(b)(1)(D)(ii).

[23]MFA section 2(b)(1)(D)(iii).

[24]MFA section 2(b)(1)(E).

[25]MFA section 2(b)(1)(F) and (G).

[26]MFA section 2(b)(1)(H).

The MFA is very clear. The minimum simplification alternative is met only if the state provides software free of charge, just as under the SSUTA. Also, if that software is "provided by certified software providers, [it] shall be capable of calculating and filing sales and use tax returns in all states qualified under this Act."[27] That is clearly the establishment of an OSS — a single compliance portal available free of charge to receive taxes for multiple jurisdictions.

With the MFA, there is a substantial compliance cost reduction for businesses and substantial risk reduction for businesses and CSPs. In terms of compliance costs, both tax calculation and return filing functionality are provided free of charge. The MFA shifts compliance risks back to the state in a manner that is perfectly in tune with *Quill.*

At its core, the Supreme Court's *Quill* decision rests on a perception of unfairness. It's unfair if a state creates an extremely complex retail sales tax (RST) regime, and then penalizes businesses if they cannot comply with the law. Under the MFA, that will change. If a state wishes to participate in the MFA and require remote sellers to collect the local sales and use tax, and if complexities remain in its sales tax regime that lead to software errors or omissions in tax calculation and reporting, then it's only fair that the state (not the taxpayer or the software provider) be held at fault.

If the MFA becomes law, and if the 45 states with a sales tax opt for either the SSUTA or minimum simplification, then only remote sellers that make less than $1 million in remote sales in the U.S. will be protected by *Quill.* That will leave international remote sellers as the major enforcement area for the states.

The U.S. states will be in exactly the same position regarding these remote sellers as the EU member states when they try to collect VAT on electronically provided services from non-EU suppliers to EU final consumers. Collection and remittance of the RST will technically be required under the MFA, but enforcement of this obligation will be nearly impossible. The U.S. states and the EU member states will be in exactly the same position. Compliance will depend on moral authority and the persuasive power of the OSS.

II. OSS in the EU

There are two OSSs in the EU and an active proposal to open up the OSS procedure to all taxpayers. Only the two limited OSSs have been adopted. In both, the goal has been to level the playing field for a defined slice of the marketplace.

A. A Limited OSS

In the late 1990s, the EU became concerned with the large volume of digital products sold to EU customers by non-EU businesses. The issue was sourcing. The Sixth Directive[28] sourced these supplies outside the EU, making them not subject to VAT. However, consumption (use and enjoyment) was occurring within the EU.[29] EU sellers of the same services were at a considerable disadvantage, with VAT rates ranging from 15 (Luxembourg) to 25 percent (Denmark).

Because the marketplace was tilted in favor of the non-EU seller, sourcing rules were changed and an OSS was adopted.

1. Sourcing Rules

Electronically supplied services from non-EU businesses were added to the list of exceptions in the earlier version of article 56, and a special rule dealing with similar business-to-consumer (B2C) transactions was added to the earlier version of article 57(1). Tax now became due in the EU because the place of supply was within the EU.

Working out the practical aspects of this change was more complicated. Business-to-business (B2B) transactions from non-EU suppliers, by far the largest part of e-commerce in monetary terms, were handled through a reverse charge procedure. B2C transactions were more difficult. Consumers don't file VAT returns, so a reverse charge wasn't possible. Non-EU businesses were simply required to collect and remit the VAT. However, there was no way to enforce this requirement.

At this juncture, the EU VAT and the RST under the MFA are in exactly the same position. Both require overseas businesses to collect and remit a destination-based consumption tax, but neither can enforce the requirement.[30] The EU sought to encourage compliance with its first OSS.

[27]MFA section 2(b)(2)(D).

[28]The Sixth Council Directive of May 17, 1977, on the harmonization of the laws of the member states relating to turnover tax — common system of value added tax: uniform basis of assessment (77/388/EEC) 1977 O.J. (L 145) 1, was repealed and replaced on Nov. 28, 2006 with the Recast VAT Directive. Council Directive 2006/112/EC on the common system of value added tax, O.J. (L 347) 1. Citations throughout this document will be to both versions. The most updated version will be referred to as the VAT Directive.

[29]The sourcing issue was the fallback rule of article 9(1) (VAT Directive, article 43). This rule provided that any service not covered in the series of exceptions that make up the rest of former article 9 were to be taxed where the supplier was located. In the case of digital services, that was frequently outside the EU and commonly in the U.S.

[30]If a business was willing to comply with the requirement to collect the VAT on B2C sales, it had two options: It could either establish itself in a member state or register in each member state where it made taxable supplies. Neither choice was optimal. Although under the first option all digital sales would be sourced to the EU jurisdiction where the business was established, the establishment process itself led to direct tax obligations. The formerly non-EU business would become an EU business for tax

(Footnote continued on next page.)

2. The One-Stop Shop

Articles 359 through 369 (formerly article 26c) were adopted. Together, they provide for an OSS that allows non-EU established businesses to select a single member state of identification where they will register (but aren't considered established). VAT from sales made throughout the EU is charged on a destination basis, and the full sum is paid over to the member state of identification on a single electronic return. The member state of identification then redistributes the VAT to the appropriate jurisdictions. Everything is required to be digital.

Although the compliance costs and risk of errors are borne by the business, filing and payment is streamlined through a dedicated Web portal established by the member state.

B. A Second Limited OSS

In 2008 the place of supply for services was generally changed from the seller's to the buyer's location. For radio and television broadcasting, telecommunications, and electronic services, that was a very significant change. Under the previous sourcing rules, it had been common for EU broadcasters to establish themselves in a low-tax jurisdiction (Luxembourg's 15 percent rate was favored) when broadcasting into high-tax jurisdictions (Denmark's 25 percent rate was avoided).[31]

This sourcing adjustment was so difficult for that industry segment that an agreement to make overall changes couldn't be reached without selectively delaying the effective date for the industry until January 1, 2015, and then further allowing the use of the OSS procedure by these firms.[32]

The implementing regulation now distinguishes between two OSSs:

- The new "union scheme" (the special scheme for taxable persons that are established within the community but not established within the member state where the services are supplied).
- The older "non-union scheme" (for taxable persons not established within the community). The regulation structures the OSS process as follows:[33]
  - — Statement: The taxable person must submit a statement to the member state where he would like to be identified (the member state of identification).[34] The member state cannot refuse the request.
  - — Updates: The statement must be updated to reflect the commencement and cessation of activity.[35]
  - — Details: The statement must indicate the taxable person's:
    - name;
    - postal address;
    - electronic address and website; and
    - national tax number (if any).[36]
  - — For a non-EU business, a statement must be provided that the person is not identified for VAT purposes within the EU.
  - — Return: A single return is required each quarter that must show:[37]
    - VAT identification number;
    - total value of supplies made in each member state;
    - total amount of VAT due in each member state; and
    - the applicable VAT rate in each member state.[38]
  - — Euros: The VAT return must be in euros (unless the member state of identification has not adopted the euro).[39]
  - — Payment: One payment will be made into the bank account designated by the member state of identification.[40]
  - — Record-keeping: Records must be kept for 10 years.[41]

and regulatory purposes. The second option also had disadvantages. Under this option, a business could conceivably be required to register in what was then 25 member states (now 27), file 25 sets of VAT returns, and do so in as many as 20 different languages. The sourcing of sales under this option would be destination based.

[31]Council Directive 2008/8/EC of Feb. 12, 2008, amending Council Directive 2006/112/EC regarding the place of supply of services, O.J. (L 144) 1 (Feb. 20, 2008).

[32]Commission Implementing Regulation (EU) No. 815/2012 of Sept. 13, 2012, laying down detailed rules for the application of Council Regulation (EU) No. 904/2010 regarding special schemes for non-established taxable persons supplying telecommunications, broadcasting, or electronic services to nontaxable persons. On October 9, 2012, the council adopted Regulation (EU) No. 967/2012 amending Council Implementing Regulation (EU) No. 282/2011 regarding the special scheme for non-established taxable persons supplying telecommunications, broadcasting, or electronic services to nontaxable persons.

[33]All taxpayer-government communications are required to be electronic.

[34]VAT Directive, articles 359 and 369b.

[35]VAT Directive, articles 360 and 369c.

[36]VAT Directive, article 364.

[37]VAT Directive, articles 365 and 369f.

[38]VAT Directive, articles 361 and 369e.

[39]VAT Directive, articles 366 and 369h.

[40]VAT Directive, articles 367 and 369i.

[41]VAT Directive, articles 369 and 369k.

The VAT paid to the member state of identification is reallocated to the appropriate member state of consumption. The taxpayer's calculation and allocation are followed. There is no unitary audit; each member state will audit on its own.

III. Two Lessons Learned

There are two lessons to be learned from a comparison of the OSSs in the MFA and the EU VAT. The first has to do with the domestic dynamic that arises when an OSS is implemented and is found to be successful: Businesses that were excluded from the OSS in the beginning seek admission later to capture efficiencies and reduce compliance risks.

Second, because the entire area of remote sellers and destination-based consumption taxes has a strong international component, the quest to level the domestic playing field eventually leads overseas. States should anticipate that foreign cooperation would be forthcoming, and they may want to prepare the way for further involvement in the U.S. sales tax. The first step in this analysis is to measure the potential revenue flows.

A. The Overcorrection Problem

The EU's OSSs are not open to all taxpayers. Only non-EU businesses selling to EU final consumers, or EU radio and television broadcasting, telecommunications, and electronic service firms can use it. The efficiency of filing a single pan-EU return through a single Web portal hasn't gone unnoticed by similarly situated businesses established in the EU.

The same situation will most likely arise under the MFA. Neither the SSUTA's nor the MFA's OSSs are open to all taxpayers. If the MFA's OSS is a success, it would be reasonable to expect a dynamic similar to that found in the EU to arise in the U.S.

In March 2004 the European Commission suggested in a consultation paper that any EU businesses making supplies (digital or otherwise) directly to EU end-users in a member state other than the state where they were established should be allowed to file under an OSS procedure.[42]

The business response to the consultation paper was overwhelmingly positive.[43] European businesses urged the expansion of the OSS system. Intra-Community B2C, domestic B2C, and even B2B transactions should be allowable, they said. The OSS was seen as a simplification that worked but had been unfairly open only to foreigners (it was later opened to EU radio and television broadcasting, telecommunications, and electronic service providers). Nevertheless, for political reasons, the proposal in the consultation paper wasn't adopted.[44]

The European Commission's shorthand expression for the current situation is that there is a mini OSS. This expression leaves open an expectation that a comprehensive OSS could be right around the corner. In fact, the commission proposes that after 2015, there should be a:

> managed broadening of the One Stop Shop over time. . . . [But] it's a good idea to wait to see the success of the mini One Stop Shop before embarking on an expansion; and this we will do.[45]

If the MFA passes and the states comply with its conditions, and they then demand that remote sellers collect the sales and use tax, it may only be a matter of time before in-state businesses request an extension of the MFA's OSS to all taxpayers (whether or not they are making remote sales). The argument will be the following: Why should an out-of-state seller be provided tax software free of charge, and be held harmless for errors, when in-state sellers are not accorded the same benefits?

This is a difficult argument to rebut in the context of a tax reform that is based on fairness. Thus, apart from aiming to level the playing field between e-commerce and brick-and-mortar businesses, as a side effect, the MFA could facilitate tax collection and compliance in

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[42]Although not clearly stated in the consultation paper, it appears that non-EU established persons would have to become established to participate. European Commission, "Consultation Paper: Simplifying VAT Obligations, the One-Stop System" (Mar. 2004), TAXUD/590/2004-EN, p. 3.

[43]*See, e.g.,* the response of Eurochambres, "Position Paper 2004: Simplifying VAT Obligations: The One-Stop System," *available at* http://www.eurochambres.be/docshare/Common/GetFile.asp?PortalSource=401&DocID=172&mfd=off&pdoc=1. Eurochambres is a 17 million-member business organization that is the sole European body serving the interests of every sector and every size of European business.

[44]The main reason this expanded OSS wasn't adopted had to do with the clearinghouse mechanism that would need to be established. According to the European Commission, the main problem was a matter of trust. Algirdas Šemeta, EU tax commissioner, indicated:

> The One Stop Shop has many merits. It can bring substantial simplification and cost reductions for businesses and member states. But for it to work in practice, *member states must trust each other* to collect the VAT on their behalf. It needs to be asked whether that degree of confidence between the member states currently exists. [Emphasis added.]

Šemeta, "The Mini-One Stop Shop for VAT — The Start of Something Big!" *World Commerce Rev.* 29 (June 2012). *See also* Sijbren Cnossen, "Commentary," in: Ian Crawford, Michael Keen, and Stephen Smith, "Value Added Tax and Excises," Ch. 4 of *Dimensions of Tax Design: The Mirrlees Review*, Institute for Fiscal Studies (Apr. 2010), at subheading "Exporter Rating System Proposed by the European Commission," at 377-382, *available at* http://www.ifs.org.uk/mirrleesreview/dimensions/ch4.pdf (discussing the political discord arising with the proposal of a clearinghouse).

[45]Šemeta, *supra* note 44, at 29.

the whole economy: Although the bill's measures target specific companies, they could potentially benefit all of them.

B. Don't Forget the International Marketplace

The second largest piece of the U.S. cross-border trade in terms of U.S. imports is European. In 2011 trade with the 27 EU member states accounted for 16.9 percent of the total value of U.S. imports, exceeded only by China at 18.8 percent.[46] In order to arrive at an estimate of the volume of international trade likely to be affected by the MFA (remote sales by businesses that exceed the MFA's $1 million threshold), we need to start with aggregate EU-U.S. trade data.[47]

Table 1 shows the number of European enterprises exporting to the U.S. in 2010, with the exception of Belgian and Irish data (these data are not available in the OECD Trading Partners database). The upper estimate of the number of EU firms that could be required to charge sales tax under the MFA is therefore approximately 146,000. These firms generated $253 billion of EU-U.S. trade value in 2010.

Under *Quill*, most of these firms would never have had an obligation to collect sales or use tax. The vast majority have no physical presence in the U.S. In 2009, 16 EU member states with 141,331 U.S.-exporting businesses reported only 15,920 U.S.-based affiliates.

There are several reasons why not all 146,000 EU exporters will want to access the private sector OSS of the MFA.

First, some firms' remote sales will not surpass $1 million. The majority of these firms will likely be micro-enterprises, usually defined as enterprises with fewer than 10 employees and turnover below €2 million. While we cannot control for turnover, the OECD Trade by Size Classes database, Rev. 4, provides information on the size class of all European firms involved in external EU trade. By identifying the percentage of micro-enterprises in the total population of exporting firms, we can get a rough idea of their number in the sub-sample of EU-U.S. exporters.

Thus, we find that 44 percent of all EU companies trading with partners outside the EU have between one and nine employees. Assuming that the percentage of micro-enterprises is similar for the sample of U.S.-exporting firms, roughly 64,800 of these firms are likely to be too small to exceed the $1 million small seller threshold.[48]

Even though almost half of all firms involved in external EU trade are micro-enterprises, they account for only 8 percent of the value of that trade. In contrast, 3 percent of companies with more than 250 employees generate 53 percent of the value of external EU trade. These larger firms and small and medium-size enterprises, or roughly 80,000 firms, are in all likelihood above the MFA threshold. Yet, for reasons explained below, that does not mean that as remote sellers, they will all be subject to state efforts to compel sales and use tax collection under the MFA. Nor does it mean that the sales and use tax on U.S. imported products is fully lost.

Second, many SMEs and large corporations active in the U.S. market already use the services of giant resellers like Digital River ($22 billion revenue) for the sale of their digital products. In fact, those resellers typically provide comprehensive services — they are a payment platform, offering both digital and physical product fulfillment, as well as marketing of the product. That means the obligation to collect the sales tax will not rest with the remote foreign seller but with the U.S. reseller. The burden of compliance would be shifted from the international party onto the domestic player in the U.S. market. Some of the sales and use tax would already have been captured in states in which a reseller is physically located.

Third, on B2B sales the U.S. buyer will most likely remit the use tax, but on B2C sales the tax is most likely unreported. That's the same pattern that plays out in the EU, where the reverse charge collects the VAT on B2B cross-border transactions but there is low compliance in a comparable B2C transaction.

It's useful, therefore, to look at the composition of European imports into the U.S. The OECD Statistics on Measuring Globalization contain a data set on bilateral trade in intermediate goods and services, with the latest recorded year being 2005 (column (5) of the table). In 2005 European exports of intermediate goods

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[46]European Commission, "United States: EU Bilateral Trade and Trade with the World" (May 2013), *available at* http://trade.ec.europa.eu/doclib/docs/2006/september/tradoc_113465.pdf.

[47]The MFA states that:

> the remote sales of 2 or more persons shall be aggregated if:
>
> 1. such persons are related to the remote seller within the meaning of subsections (b) and (c) of section 267 or section 707(b)(1) of the Internal Revenue Code of 1986; or
> 2. such persons have 1 or more ownership relationships and such relationships were designed with a principal purpose of avoiding the application of these rules.

MFA section 2(c)(1) and (2).

These conditions eliminate incentives for the establishment of multiple sister companies without physical presence by the parent or other subsidiaries, whose goal would be to maintain sales below the threshold and thus, avoid the collection of sales tax.

[48]This assumption is strongly supported, as it is possible that micro-enterprises are mostly trading with partners in close geographical proximity to the EU, whereas big exporters are engaged in overseas trade.

Number of EU Enterprises Exporting to the U.S. and Value of Exports, 2010

Country	(1) Total number of enterprises exporting to the U.S.	(2) Wholesale, retail trade, and repair, number of enterprises	(3) Value of trade in mil USD (total number of enterprises)	(4) Value of trade in mil USD (wholesale, retail trade, and repair)	(5) Value of intermediate goods and services in mil USD, 2005
Austria	2,694	893	6,225.79	631.063	4,074.169
Bulgaria	725	197	277.733	41.149	228.8975
Cyprus	143	51	15.733	1.66	305.0888
Czech Republic	2,166	578	1,813.47	201.9	1,689.441
Denmark	3,175	1,213	5,944.5	1,208.34	4,963.871
Estonia	251	54	431.341	7.475	198.8327
Finland	1,758	427	4,633.74	63.611	2,367.472
France	19,251	6,478	28,533	4,398.48	20,037.14
Germany	20,795	5,705	77,481.1	3,085.18	45,526.91
Greece	2,422	770	1,533.11	78.682	5,155.519
Hungary	1,243	328	1,986.17	651.78	1,380.397
Italy	29,129	7,075	25,457.3	2,473.95	18,274.61
Latvia	274	70	120.671	13.079	177.363
Lithuania	384	106	558.691	19.153	196.442
Luxembourg	157	82	376.932	11.3	631.1612
Malta	147	37	258.335	23.483	246.5662
Netherlands	5,617	2,101	18,523.5	5,640.39	8,649.117
Poland	3,625	911	2,549.36	292.132	1,548.474
Portugal	2,236	544	1,723.08	94.134	1,534.645
Romania	792	155	652.963	17.317	943.69
Slovakia	481	98	899.616	11.849	334.3952
Slovenia	493	86	360.418	6.669	229.232
Spain	11,360	3,393	8,269.75	1,301.47	7,666.638
Sweden	6,351	2,126	11,268.9	471.939	7,825.544
United Kingdom	29,554	10,217	53,417	6,337.45	40,226.83
Total	145,178	43,695	253,312.2	27,083.64	198,177.5

Source: OECD Trading Partners Database, Rev. 4; OECD Bilateral Trade in Intermediate Goods and Services.

and services to the U.S. were $198 billion, or 63 percent of the value of total exports to the U.S. in 2006.[49] As noted above, a large portion of the use tax on these B2B sales may already be collected. Nevertheless, the remaining 37 percent of trade value is likely generated by B2C transactions, which implies significant foregone sales tax revenue.

Apart from intermediate goods, we can disaggregate EU exports to the U.S. by sector, the most interesting being wholesale, retail trade, and repair (columns (2) and (4) of the table). In 2010, 30 percent of all European exporters conducted wholesale or retail trade with the U.S., amounting to $27 billion, or 10 percent of total value.

Quill is not dead. Currently, international traders without a physical presence in the U.S. have no obligation to collect the sales and use tax barring:

- passage of the MFA (or another similar federal statute);
- state membership in the SSUTA or satisfaction of minimum simplification requirements; and

[49]The earliest available year with data for the value of European exports to the U.S. is 2006, in the OECD Trading Partners database, Rev. 3. The calculation of the percentage excludes data for Bulgaria, Germany, Greece, Malta, the Netherlands, Spain, and the U.K., all of which have missing observations for the value of trade with the U.S. for 2006.

- a state statute requiring remote sellers to collect the sales and use tax on in-state sales.

If the MFA becomes law, and if the use tax on imported intermediate and B2C goods is partially collected, it is reasonable to assume that the international slice of U.S. trade will contribute significantly to rising sales tax revenue. However, it's likely that many international firms would outsource the service of sales tax collection to U.S. resellers, so the obligation to comply with state tax laws may ultimately reside with U.S. businesses. Nevertheless, if approximately 80,000 EU businesses exceed the $1 million remote sale threshold, and if these firms are making more than $200 billion in U.S. sales, it's likely that a significant amount of the recovered sales and use tax revenue will come from the international slice of the unbalanced U.S. marketplace.

IV. Conclusion

The EU and the U.S. states are looking at much the same problem when they endeavor to have remote sellers collect and remit destination-based consumption taxes. Both systems recognize that simply having a law in place requiring collection is insufficient. Both systems have adopted OSSs and compliance simplifications to encourage or persuade remote sellers to comply. The EU's preference for a government-centric OSS and the U.S. preference for OSSs that involve third parties and certified software may have very different success profiles. This is an important assessment that is yet to come, but it suggests that the U.S. may want to borrow a solution from the EU, or the EU may want to borrow a solution from the U.S. states. Both sides need to be open to that possibility.

It's clear that there is room for considerable international cooperation. EU Tax Commissioner Algirdas Šemeta indicated that the European Commission is anxious to cooperate. He observed:

> There is no effective way of ensuring compliance if a business located in California, for example, provides e-services to a private individual in Slovakia and does not register for the e-commerce scheme and pay Slovak VAT. What can the national tax authorities do realistically? *The Commission is addressing this issue and has asked member states for a mandate to negotiate with third countries on this issue from a collective position of power.* For the time being, though, compliance depends on the willingness of suppliers in third countries to assume their legal obligations.[50] [Emphasis added.]

If the EU is concerned about a remote seller in California making sales into Slovakia, then the California State Board of Equalization is likely equally concerned about a remote seller in France making sales into Los Angeles.

Cooperation could be government to government, but it could also be through software certification. If the EU adopted the March 2004 consultation paper proposal and moved generally to OSS compliance, and if the EU decided to adopt the private sector software model advanced by the SSUTA and MFA, then it would be a relatively easy matter to jointly certify global software platforms that would comply with all U.S. and EU transaction taxes.

There are already a number of certified software packages in the U.S. that are fully compliant with the thousands of U.S. RST jurisdictions. Some of these packages are also fully compliant with the EU VAT. Joint EU-SSUTA certification may be just ahead if the MFA proves to be a success at persuading remote sellers to comply with collection obligations. It would certainly be a software solution that would be in high commercial demand for the businesses engaged in transatlantic trade — the largest and wealthiest market in the world that accounts for more than 54 percent of world GDP in terms of value and more than 40 percent in terms of purchasing power. ◆

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[50]Šemeta, *supra* note 44.

Statement for the Record

Scott Appel,
President and Chief Executive Officer
Touch of Color Design

to the

House Judiciary Committee

March 4, 2014

Chairman Goodlatte, Ranking Member Conyers and Distinguished Members of the Committee, my name is Scott Appel. I thank you for this opportunity to provide this written testimony in support of the Marketplace Fairness Act ("MFA"). The Act is of great importance to me as an owner and operator of a brick and mortar retail business and is crucial to allow me to compete fairly with Internet sellers.

I am the president and owner of three design centers; one in Harrisburg, one in Philadelphia and one in Pittsburgh. These stores sell flooring to designers, remodelers, and custom builders. In addition, I own and operate two Big Bobs Flooring Outlets; one in Harrisburg and the other in Lancaster, Pennsylvania that sell flooring to the general public. I have 56 local employees in my stores and I engage numerous local independent contractors to install his products. For the Committee's convenience, I have listed the stores and their locations as an attachment to my statement.

I submit this written testimony to explain the need for the Marketplace Fairness Act. My testimony is based on personal experience as a local brick and mortar retailer.

I. Unfair Competition by Internet Sellers

I recognize the Internet as a significant and often positive factor in the American economy. It provides consumers with information on the types of products available and allows comparative shopping. I have myself embraced the Internet, developing websites for my stores, blogging on new products, advertising and using social networking. Accordingly, all I seek is to have a fair chance to compete with my online competitors, not inhibit this competition.

The problem is the inability of states like Pennsylvania to enforce their sales tax laws to include Internet sales. This, in turn, gives the Internet seller an unfair advantage. This is not hypothetical for the flooring industry. Internet sellers actively advertise no sales tax. Flooring is a high-ticket item costing thousands of dollars. As result, consumers generally want to see and

touch the flooring before purchasing. With increasing frequency, I have customers come in with printouts of products that they can buy online. Consumers are always looking for a deal, and they are shopping online for more and more products every day. It does not matter if the consumer was previously one of my company's customers; the customer still seeks a lower price even if from a faceless Internet seller. While my stores can compete with the Internet sellers if we were playing by the same rules, the sales tax often makes a big difference. Given that flooring is an expensive product, sales taxes are hundreds of dollars. Since these Internet retailers literally tell consumers that they are not required to collect sales tax, it gives them an unfair advantage. Internet retailers can now poach the local shopper and rob his state of much needed sales tax revenue.

For example, in just the past month, one of my Big Bob's Flooring Outlet stores sold a 700 square foot hardwood floor job to a customer for no profit just to take avoid losing the deal to an Internet seller. The difference between making a profit and not was the 6% sales tax that I had to collect—the tax that the Internet seller advertises does not have to be paid. This adversely affects retailers like me and inhibits my ability to sustain a healthy gross profit margin, which allows me to pay better than average wages and benefits to my employees. These unfairly lost sales also affects my ability to earn enough net profit to continue to invest in my stores, build new stores and add employment and income to our communities. If this trend continues, with Internet sellers having an unfair advantage with a "no sales tax" discount, the local brick and mortar independent flooring retailers will be driven out of business.

Internet sales of flooring are increasing rapidly, especially with the introduction of easy to install floors. Today, a consumer can install a laminate floor without any glue or nails, and simply snap it together. Similarly, there are self-adhesive laminates, tiles and vinyl that can be installed by simply peeling off the back sheet and laying the floor tile in place. Shaw and Mohawk, the two largest manufacturer of carpet, sell self-stick carpet tiles, making installation of wall-to-wall carpet easier. There are even systems to allow easy installation of hardwood floors, such as the Elastilon Strong Self Adhesive Hardwood Floor Install System. There are a variety of other flooring products that a consumer can buy and install him or herself. The problem is not the availability of these products, but that Internet sellers are selling them with no sales tax, creating an unfair and unearned advantage over local brick and mortar stores.

The MFA provides a fair solution to this problem. The Act allows, but does not require, a state to have Internet sellers collect the sales tax just like local retailer do now. The Act puts the decision where it belongs, at the local and state level. Sales taxes are set at the state level to provide for local services and programs. These taxes pay for fire and police departments, libraries, parks and a host of other local projects and services. Who better to make the decisions on whether to have a sales tax, to set the amount and to determine how the use the revenue than the local officials who are directly elected by local constituents? Unless Congress acts, however, these taxes cannot be effectively collected on Internet sales. The loss of the sales tax revenues from Internet sales can only lead to higher taxes to support these local services and programs.

II. House Judiciary Committee Basic Principles

I have addressed below the "Basic Principles on Internet Sales Tax" set forth by the Committee on September 18, 2013.

1. Tax Relief

The MFA allowing states to have Internet sellers collect the existing sales tax does not create a new tax. The consumer owes the sales the tax on all items he or she purchases whether at a local store or from a remote Internet seller. The problem is there is no practical way to collect the tax unless the seller collects it at the time of the sale. That is why the local retailer is obligated to collect the tax on all of its sales. The MFA simply authorizes states to require that remote Internet sellers collect sales tax from its customers, just like the local brick and mortar store now do. Accordingly, the MFA does not create a new tax anymore than enforcing existing tax laws creates a new tax. Rather, it simply creates a practical means of collecting the taxes that are already due.

2. Tech Neutrality

Requiring brick and mortar stores to collect sales taxes, while exempting online businesses from the same requirement does not put competitors on equal footing. Brick and mortar stores are at a distinct disadvantage. In essence, out-of-state Internet sellers have a "no sales tax discount" that these online sellers advertise as a reason to buy from them and not your local brick and mortar store. Local brick and mortar stores must collect the tax, and that discount is often the difference between the local stores making or losing a sale. The MFA, therefore, is essential for a fair free market to work in the flooring industry—it allows all competitors to operate under the same rules.

3. No Regulation Without Representation

The Internet seller is not paying the sales tax. Rather, the tax is paid by the consumer. These taxes are determined at the state and local level and are used to support local services and needs, such as fire and police departments, libraries and parks. The consumer, whether he or she buy locally or from a remote Internet seller, lives in the locations where the tax is due and benefits from the services for which these taxes pay. Requiring an Internet seller to collect the tax from these consumers is only fair. All that the MFA would do is authorize states to require Internet sellers collected the tax so that the local consumer simply pays his or her fair share of the local sales tax for the items purchased regardless of where or how they were bought.

4. Simplicity

The requirement for out-of-state sellers to collect the sales tax does not impose any real burden. The collection is not complicated with today's computer system. In Pennsylvania, businesses remit sales tax electronically using an approved third party software vendor. I have different sales taxes at my Harrisburg, Philadelphia and Pittsburgh stores. There is no problem with changing the right amount as the software automatically calculates the correct sales tax that is due.

An Internet seller is already savvy with computer systems, using them to get authorization for credit cards, to verify addresses for shipment, to track deliveries and to advertise their product online. Calculating the sales tax takes nothing more than entering the customer's address. Every online seller already gathers that information done at the time of sale in order to deliver the product to the customer. Moreover, the MFA would require a state to

meet the standards for simplifying their sales tax rules, provide the Internet seller free software to implement the collection and remittance of the sales taxes that are already due on these sales, and allow Internet and mail order sellers to elect to register with the "one stop" system covering all participating states. Accordingly, it costs nothing, is easy to use and uses the consumer's address the Internet seller already collected.

Compliance is sufficiently simple to allow any small business to comply. The current MFA includes an unnecessary small business exception for any entity with less than $1 million of Internet sales. This is far too large of an exemption. A $1 million is approximately the size of the gross sales of the average retail flooring dealer in the United States. There simply is no need for a small business exception.

5. States' Rights

State and local governments determine whether to have a sales tax and the amount of the tax. These taxes support the state and local services and projects. The MFA does not require a state to implement a sales tax. To the contrary, the Act leaves it to the states and local jurisdictions to decide whether to implement a sales tax, the amount of the tax, if any, and even whether to participate the MFA and have remote sellers collect the tax.

6. Privacy Rights

I am unaware of any privacy issues raised by the MFA. As a local retailer, I already collect sales taxes without violating any privacy right of my consumer. Internet sellers' collecting sales taxes would create no new privacy concerns.

III. Conclusion

The MFA is needed to ensure fair competition, a cornerstone of the America capitalism, and to allow states to effectively collect the taxes that are already due on Internet sales. Without it, local retailers like me will continue to suffer, local jobs will be lost, tax revenue already owed will not be collected and local communities will suffer. The MFA offers a fair solution without imposing unfair burdens on Internet sellers. To the contrary, the Act will allow a level playing field for all competitors, whether a brick and mortar store, exclusively an online retailer or a brick and click business.

Attachment 1

Store Locations

Big Bobs Flooring Outlet
820 Plaza Blvd
Lancaster, PA 17601
Pennsylvania 16th District: Rep. Joe Pitts

Big Bobs Flooring Outlet
6305 Allentown Blvd
Harrisburg, PA 17112
Pennsylvania 11th District: Rep. Lou Barletta

Touch of Color Design Group
6303 Allentown Blvd
Second Level
Harrisburg, PA 17112
Pennsylvania 11th District: Rep. Lou Barletta

Touch of Color Flooring
6303 Allentown Blvd
Harrisburg, PA 17112
Pennsylvania 11th District: Rep. Lou Barletta

Touch of Color Flooring
4075 Windgap Ave
Pittsburgh, PA 15204
Pennsylvania 13th District: Rep. Michael Doyle, Jr.

Touch of Color Flooring
270 E Geiger Rd.
Philadelphia, PA 19115
Pennsylvania 17th District: Rep. Allyson Schwartz

NATIONAL CONFERENCE *of* STATE LEGISLATURES

The Forum for America's Ideas

STATEMENT OF

SENATOR SHARON WESTON BROOME, LOUISIANA
SENATOR DEB PETERS, SOUTH DAKOTA
CO-CHAIRS, NCSL STEERING COMMITTEE

ON BEHALF OF THE

NATIONAL CONFERENCE OF STATE LEGISLATURES

REGARDING

"Exploring Alternative Solutions on the Internet Sales Tax Issue"

BEFORE THE

COMMITTEE ON JUDICIARY
UNITED STATES HOUSE OF REPRESENTATIVES

MARCH 12, 2014

COMMITTEE ON JUDICIARY
UNITED STATES HOUSE OF REPRESENTATIVES

March 12, 2014

Statement of

Senator, Sharon Weston Broome, Louisiana
Senator Deb Peters, South Dakota
Co-Chairs, NCSL Steering Committee

National Conference of State Legislatures

Chairman Goodlatte, Ranking Member Conyers, and members of the Judiciary Committee, we are pleased to submit this statement on behalf of the National Conference of State Legislatures (NCSL) and respectfully request that you submit it for the record. The National Conference of State Legislatures is the bipartisan national organization representing every state legislator from all fifty states and our nation's commonwealths, territories, possessions and the District of Columbia.

We are pleased that the Judiciary Committee is committed to exploring the issue of remote sales tax collection to determine a legislative solution that would level the playing field for all retailers and would allow states the authority to collect taxes they are already owed. We believe that your efforts, coupled with the passage of legislation by an overwhelming bipartisan Senate vote last year to allow states to require the collection of sales taxes on remote transactions, will ensure that this tax compliance issue will be fixed before the next holiday buying season. We also want to acknowledge the leadership of your colleagues, Congressman Steve Womack of Arkansas, Congresswoman Jackie Speier of California, and over 65 members of Congress in sponsoring the Marketplace Fairness Act.

Fixing the remote sales tax collection loophole is the top priority of NCSL and has been for over a decade. This loophole, developed as a result of two Supreme Court decisions, has resulted in growing losses of revenues for state and local governments and has created an unlevel playing field for our main street and community retailers. NCSL advocates for passage of e-fairness legislation because it levels the playing field for local businesses, which are the economic backbones of our communities, and protects an important revenue stream for state and local governments to provide vital services. As sales taxes **account for over a third of revenues for most states**, including over **half of tax collections for six states**, the inability to collect taxes that are legally owed constrains states' options to reform their tax code elsewhere. This includes lowering tax rates or requiring states to raise certain tax rates to fund necessary government services.

Additionally, the recent recession has had a debilitating effect on state budgets. According to NCSL's survey of state legislative fiscal officers, between FY 2008-2013, states closed a cumulative $527.7 billion budget gap, primarily through program reductions. Raising taxes in the sluggish economy remains an unviable option for most states, so closing the sales tax compliance problem could provide states with the option of using some of the additional revenue to offset federal spending reductions.

In the absence of federal action, states have sought solutions to the remote sales tax loophole in order to protect their budgets as well as their main street retailers. Over half the states have enacted legislation to respond to the concerns raised in the Supreme Court decisions to remove the burden and cost on out of state sellers to collect and remit sales taxes, a number of states have enacted affiliate nexus or "Amazon" laws, some have increased reporting requirements on retailers, and others have tried other mechanisms to collect the taxes they are already owed. Unfortunately, state attempts alone will not solve the problem; it must be solved by Congress.

Moreover, states have also adopted policies contingent upon passage of a federal bill, including plans to use the money to lower other taxes or eliminate them altogether. States have also obligated the money to programs that were drained of funding during the Great Recession, such as infrastructure and transportation investment.

As you are aware, NCSL was instrumental in crafting the Streamlined Sales and Use Tax Agreement, which addresses the concerns of the United States Supreme Court in the *Quill v. North Dakota* Case in 1992. Today, 24 of the 45 states that levy sales taxes are members of the Agreement, which has proven that remote sales tax collection is not only possible, but that it can be done with no additional burdens being placed on remote retailers. However, we acknowledge that it is unlikely that every state will enact simplifications required by the Agreement and that an alternative method must be considered to address remote sales tax collection in every state.

As the committee considers alternative proposals, NCSL stands ready to work with you and your staffs to provide solutions that will allow states to collect taxes without inhibiting the burgeoning sector of electronic commerce. However, doing nothing will continue to jeopardize your main street sellers and the millions of Americans employed by these small businesses. Please find the attachments which detail state revenue losses from remote commerce in FY 2012 and also outline state activity in the area of remote sales tax collection.

Thank You.

Attachment 1

Combined State & Local Revenue Losses Remote Commerce – 2012[1]

	All Out of State Electronic Sales	All Out of State Sales
Alabama	**170,400,000**	**347,734,399**
Alaska	1,500,000	3,035,981
Arizona	**369,800,000**	**708,628,254**
Arkansas	113,900,000	236,311,930
California	**1,904,500,000**	**4,159,667,947**
Colorado	172,700,000	352,563,574
Connecticut	63,800,000	152,367,405
District of Columbia	35,500,000	72,517,182
Florida	**803,800,000**	**1,483,690,010**
Georgia	**410,300,000**	**837,610,389**
Hawaii	60,000,000	122,514,495
Idaho	**46,400,000**	**103,120,482**
Illinois	**506,800,000**	**1,058,849,588**
Indiana	195,300,000	398,817,708
Iowa	**88,700,000**	**181,012,560**
Kansas	142,900,000	279,224,028
Kentucky	109,900,000	224,484,309
Louisiana	**395,900,000**	**808,311,357**
Maine	32,100,000	65,430,824
Maryland	184,100,000	375,944,240
Massachusetts	131,300,000	268,002,460
Michigan	**141,500,000**	**288,954,339**
Minnesota	235,300,000	455,219,250
Mississippi	134,900,000	303,286,360
Missouri	**210,700,000**	**430,191,928**
Nebraska	61,300,000	118,052,068
Nevada	168,900,000	344,923,618
New Jersey	202,500,000	413,390,425
New Mexico	120,500,000	245,989,786
New York	**865,500,000**	**1,766,968,251**
North Carolina	**213,800,000**	**436,517,492**
North Dakota	15,300,000	31,274,219
Ohio	**307,900,000**	**628,613,189**
Oklahoma	140,800,000	296,348,658
Pennsylvania	**345,900,000**	**706,241,542**
Rhode Island	**29,000,000**	**70,436,458**
South Carolina	**124,500,000**	**254,290,538**
South Dakota	29,800,000	60,826,849
Tennessee	**410,800,000**	**748,480,889**
Texas	**870,400,000**	**1,777,090,593**
Utah	**88,500,000**	**180,658,961**
Vermont	25,100,000	44,759,329
Virginia	**207,000,000**	**422,651,971**
Washington	**281,900,000**	**540,968,704**
West Virginia	50,600,000	103,284,206
Wisconsin	**142,100,000**	**289,006,114**
Wyoming	28,600,000	61,744,705
Total	**11,392,700,000**	**23,260,009,564**

[1] *Source: Dr. Donald Bruce & Dr. William Fox, Center for Business & Economic Research University of Tennessee*

Attachment 2

State Activity to Collect Remote Sales

Streamlined Sales Tax (SST) States

The Streamlined Sales and Use Tax Agreement was created by the National Governor's Association (NGA) and the National Conference of State Legislatures (NCSL) in the fall of 1999 to simplify sales tax collection. Streamlined has proven that remote sales tax collection is not only possible, but can be done very efficiently, without creating an undue burden on retailers. Since 2005, streamlined states have collected over $1 billion in taxes remitted voluntarily by retailers.

The states that have joined SST are:

Arkansas; Georgia; Indiana; Iowa; Kansas; Kentucky; Michigan; Minnesota; Nebraska; Nevada; New Jersey; North Carolina; North Dakota; Ohio; Oklahoma; South Dakota; West Virginia; Rhode Island; Utah; Vermont; Washington; Wisconsin; Wyoming.

Expanded Nexus/Affiliate Nexus

In 2008, New York State passed the nation's first "affiliate nexus law," which declared that the connection between a remote vendor and an in-state entity, which performs certain work that can be attributed to the remote vendor, constitutes nexus in the state. Thus, the remote vendor would now be required to collect and remit New York sales tax.

Since 2008, other states have enacted legislation that expanded the definition of "nexus" in an effort to collect the taxes they are owed. While the laws' effectiveness vary by state, generally, states have not come close to collecting anticipated revenue. In fact, some states may have lost money after enacting "affiliate legislation" as a consequence of out-of-state vendors severing their relationships with in-state entities. In such instances, the state was still unable to collect the owed taxes and many in-state entities, which saw declining revenues due to the severance of the contract with the remote vendor, reported less income tax.

States that have expanded their definition of nexus are:

Alabama; Arkansas; California; Georgia; Illinois; Iowa; Kansas; Maine; Minnesota; Missouri; New York; North Carolina; Pennsylvania; Rhode Island; South Dakota; Vermont; West Virginia.

Individual State Actions

In addition to joining SST and expanding the definition of "nexus," states have also tried other mechanisms to collect remote sales taxes and have also allocated expected funding to specific areas, including tax reduction and infrastructure spending.

Tax Reduction

Arizona

House Bill 2465 passed the House Ways and Means Committee in February and awaits consideration by the Rules Committee before being considered by the full House. It would require state tax authorities to determine how much in new sales taxes were collected in out of state sales including those made online in the first year and reduce the following year's income tax rate by the same amount.

Iowa

"I want to be transparent in my intentions regarding any additional revenues if the Marketplace Fairness legislation ultimately becomes law -- I intend to utilize any related revenue that the State would receive to enable further tax relief to Iowans, including income tax reductions."

– Governor Branstad in a Letter to Representative Steve King

Maine

"I have pledged to lower Maine income taxes and stop wasteful government spending. One powerful tool in achieving these goals would be to have the ability to collect taxes that are already due."

– Governor LePage in a Letter to Senators Olympia Snow and Susan Collins

Missouri

In 2013, Governor Jay Nixon vetoed legislation that would have made any revenue collected from federal remote sales tax legislation be offset with reductions to the personal income tax. The issue is again under consideration in 2014.

Ohio

In 2013, Governor Kasich signed into law a budget that would dedicate all revenues from federal e-fairness legislation to reducing their state's income tax.

Rhode Island

In his state of the state address on January 15, Governor Chafee proposed to lower the corporate income tax rate from 9 percent to 6 percent contingent on whether Congress allows states to collect the sales tax on purchases made through out of state sellers including those made online.

Utah

In 2013, Utah enacted Senate Bill 58, which creates a restricted account for all sales tax revenue collected from online merchants and suggests the revenue be used to cut taxes.

Tennessee

Governor Bill Haslam, House Speaker Beth Harwell, and Senate Speaker Ron Ramsey, all support the Marketplace Fairness Act and have indicated that they would like to use some of the revenue generated from online sales tax collection toward reducing current state taxes.

Wisconsin

In 2013, Governor Walker signed into law a budget that would dedicate all revenues from federal e-Fairness legislation to reducing their state's income tax.

Infrastructure Funding

Maryland

The enacted transportation bill of 2013 depends on e-fairness revenue for transportation funding. If a federal bill does not pass by January 2015, an additional gas sales tax is triggered.

Virginia

The enacted budget of 2013 depends on e-fairness revenue for the transportation plan's funding. If a federal bill does not pass by January 2015, the wholesale gas tax will increase 1.7% to cover additional funding cost.

Reporting Requirement

Colorado

Enacted in February 2010, Colorado requires online retailers to provide a detailed purchase report, by January 31 of each year, to customers with made more than $500 of annual Colorado purchases the previous year. Colorado also requires the remote retailers to provide a summary purchase report, with the total amount of each customer's annual Colorado purchases, to the Colorado Department of Revenue by March 31. This law is currently the subject of a legal challenge brought

by the Direct Marketing Association and others. In the meantime, the U.S. District Court has suspended enactment of the law while the legal challenge proceeds.

Oklahoma

Enacted in June 2010, retailers selling into Oklahoma are required to provide notice to consumers who may owe use tax on the purchase.

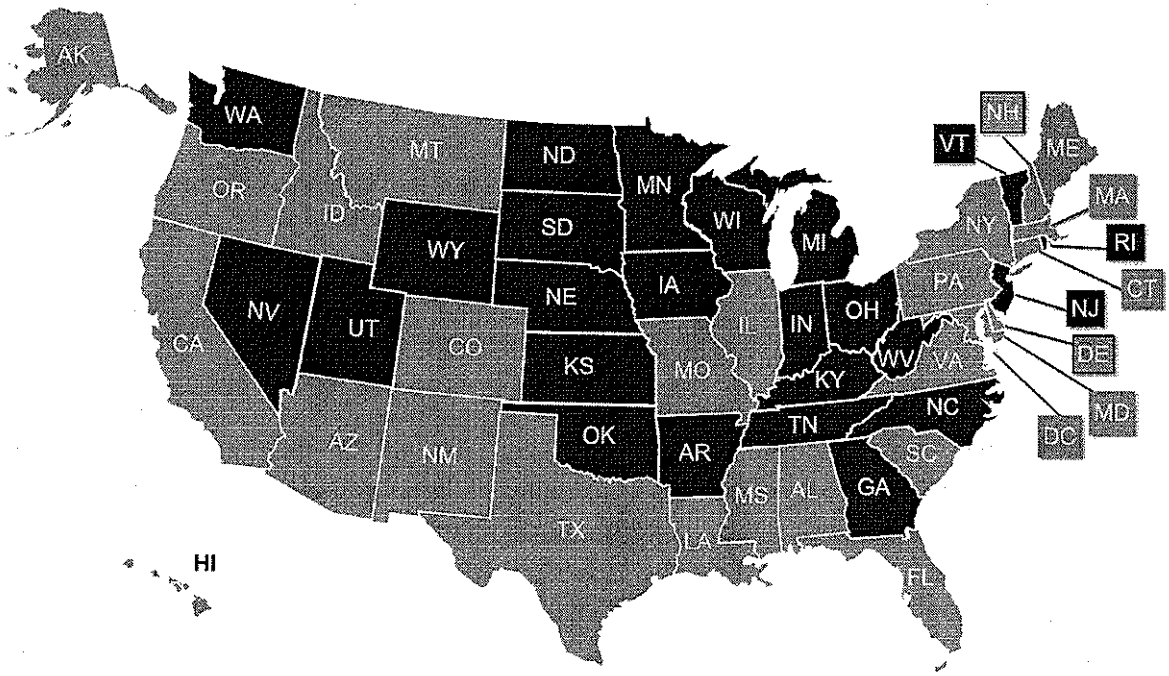
South Dakota

Enacted in April 2011, retailers selling into South Dakota are required to provide notice to consumers who may owe use tax on the purchase.

Vermont

Enacted in May 2011, retailers selling into Vermont are required to provide notice to consumers who may owe use tax on the purchase.

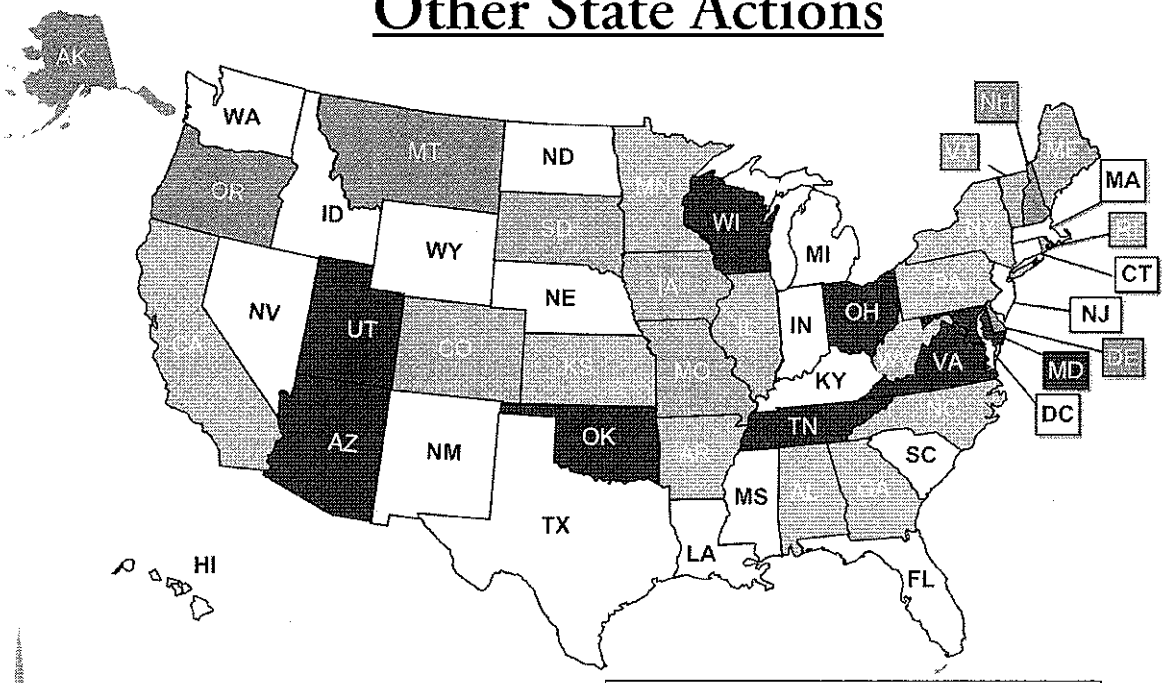
Streamlined Sales Tax States



LEGEND

- States that have joined SST
- States that have not joined SST
- States with No Sales Tax

Other State Actions



LEGEND

- Expanded/Affiliate Nexus
- Individual State Initiatives
- Multiple State Initiatives
- States with No Sales Tax

FEDTAX

STATEMENT SUBMITTED FOR THE RECORD TO

THE UNITED HOUSE OF REPRESENTATIVES
COMMITTEE ON THE JUDICIARY
FULL COMMITTEE HEARING

EXPLORING ALTERNATIVE SOLUTIONS ON THE INTERNET SALES TAX ISSUE

MARCH 12, 2014

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TaxCloud

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INTRODUCTION

Chairman Goodlatte, Ranking Member Conyers, and distinguished members of the Committee on the Judiciary, thank you for the opportunity to submit this Statement for the Record on this hearing, "Exploring Alternative Solutions on the Internet Sales Tax Issue." Our company, FedTax, is the proud inventor and operator of TaxCloud, a free online sales tax compliance service now being used by approximately 5,000 online retailers of all sizes. TaxCloud is available at no cost to retailers because we are a Certified Service Provider (CSP) for the twenty-four Member States of the Streamlined Sales and Use Tax Agreement (SSUTA). Our company was founded in 2008 by technology executives with decades of experience building some of the most recognizable brands in e-commerce. At our previous companies we experienced firsthand how difficult sales tax compliance can be, and we made it our mission to make sales tax compliance easy for businesses and more efficient for state and local governments. As we have grown, our executive team has expanded to include payments industry executives as well as nationally recognized sales tax and public policy experts.

In his opening remarks, Chairman Goodlatte named several technology-related fears regarding the Marketplace Fairness Act that we are uniquely qualified to address: technical capabilities of the prescribed free software, integration costs related to the free software, concerns for the direct mail industry, and concerns related to additional audit exposure.

We agree that Chairman Goodlatte's stated concerns are important, and we are convinced that they can (and should) be addressed.

BACKGROUND

This testimony is not based upon hypothetical notions or unproven theories. Rather, it is informed by our direct experience as a SSUTA CSP since 2010.

A brief background: SSUTA's goal is to minimize or eliminate the burdens of sales tax compliance for businesses. Since its inception in 1999, it has sought input from state and local governments as well as the business community through regularly scheduled public meetings.

During its first few years, SSUTA stakeholders publicly debated many different sales tax modernization and simplification schemes (a subset of which have been proposed before the committee today). Ultimately, they agreed on an approach that relied upon modern technologies to accommodate the many nuances and variations in sales tax law across state and local governments.

Over the next few years, the SSUTA states developed the Certified Service Provider program, including the policies, practices, and procedures to be employed by each of the participating states to test and verify that a CSP candidate's software and/or service adhered not only to SSUTA's rules (including sourcing, taxability, rounding rules, etc.) but also to each state's statutes. Today, six companies (including ours) have achieved CSP designation. It should also be noted that achieving CSP designation is not a one-time event but an ongoing process; our systems are regularly tested, verified, and audited by the states to maintain our certified status.

During this time, SSUTA stakeholders also worked with the tax technology group TIGERS[1] to develop standard formats for states to provide open source sales tax rate and jurisdictional boundary data for use by the business community. The work with TIGERS also included the specification and adoption of a Simplified Electronic Return (SER), based upon the widely used e-file format.

The current SSUTA Member States represent more than half of the states with sales and use tax laws, including Arkansas, Georgia, Indiana, Iowa, Kansas, Kentucky, Michigan, Minnesota, Nebraska, Nevada, New Jersey, North Carolina, North Dakota, Ohio, Oklahoma, Rhode Island, South Dakota, Tennessee, Utah, Vermont, Washington, West Virginia, Wisconsin, and Wyoming.

In these SSUTA states, each of the CSPs already manages all aspects of sales tax compliance for their respective retailers. These responsibilities include:

1. Calculation of applicable sales tax rates (including state, county, city, and special jurisdictions)
2. Application of any full or partial product-based exemptions
3. Capturing any available use-based exemptions
4. Detailed jurisdictional (and sub-jurisdictional) reporting of sales tax collections
5. Automated, timely filing of sales tax returns
6. Automated remittance of sales tax proceeds to applicable jurisdictions
7. Primary response to any jurisdictional audit inquiries

Technical Capabilities

Some have suggested that systems capable of keeping track of the sales tax laws of over 9,600 jurisdictions simply do not exist, or that the technologies necessary to achieve compliance would be prohibitively costly for small businesses. TaxCloud's direct work with taxpayers refutes these assertions. It doesn't matter if there are 9,600 or 96,000 jurisdictions; modern e-commerce systems are adept at easily managing such diversity, as Joe Crosby noted in his testimony before the committee. Businesses do not need to spend enormous quantities of time or resources to achieve compliance.

Integration Costs

Even with free software already available, opponents continue to complain that businesses will be burdened with the costs of integrating such software into their existing systems. This line of argument ignores the reality that all but the very largest retailers (and a few retailers who rely on legacy systems) rely upon pre-written software and/or online hosted platforms for e-commerce and

[1] The Tax Information Interchange Task Group of ANSI ASC X12 was formed in 1991, and initially worked with traditional EDI formats. The Task Group produced X12 standard Transaction Set 813, the generic EDI tax filing, which is still in use today in the Motor Fuel and Sales Tax areas. TIGERS began working with XML in December 2000, and issued its first production schema set in 2003.

The task group became "TIGERS" in December 1994, with the realization that technical standards were not enough - states and their partners needed guidance and assistance in turning the standards into actively supported electronic commerce programs. The group broadened its scope to include peer reviews of state technical implementations and mappings, guidance in technical infrastructure for e-commerce, and model documentation for the business rules enforced by the state programs.

order management. Retailers rely upon these systems to avoid the costs of developing, managing, and maintaining such systems on their own, costs that are magnified by the changing nature of e-commerce, which is constantly responding to evolving cyber-crime threats, payments and security industry best-practices, and, yes, even legislative requirements. When their retailer clients need to collect sales tax, platform vendors will provide ways for them to do so, embedded within the platforms that retailers already use.

E-commerce platform vendors are intensely competitive and focused; they take pride in not only complying with evolving requirements but often surpassing them, occasionally with stunning results. For example, much of the cloud computing infrastructure now transforming every corner of the technology sector can be traced to several of the largest e-commerce companies adapting to comply with the Sarbanes Oxley Act of 2002. There is no reason to believe these e-commerce platform vendors will not respond to action by Congress in an equally competitive manner to provide sales tax management services for their clients. In fact, this process is already underway—almost all of the most widely used e-commerce and order management platforms have already adopted and integrated with one or more CSPs.

Direct Mail Concerns

Some direct mail businesses are concerned that they could be required to include within their mail order catalogs a very long insert with every possible sales tax rate in the country. But mail order catalogs are designed to be mailed to their customers, so each customer's mailing address can be harnessed to solve this problem. Just as the catalog vendor prints each customer's address on each catalog, there is no reason they couldn't print the effective sales tax rate for that specific address right on the mailing label!

Leveraging the address block for other customer-specific data is a technique routinely practiced in the direct mail industry today. Most mail order catalogs already print customer-specific Customer Reference or Quick Service Numbers (usually 5 to 9 characters), which the customer conveys to a sales agent when placing a phone order or enters on the website when placing an online order.

Furthermore, most catalog retailers encourage their customers to place their orders online or by phone; many don't even offer paper ordering forms any longer. Of course, once a customer "channel shifts" from the printed catalog to an online storefront or telephone order, both of these ordering systems can rely upon free software and services provided by the states to determine the correct sales tax rates and even apply any available item-level exemptions.

If a catalog exemption is to be included, it should be carefully crafted so as not to favor catalog retailers over other remote retailers (or local retailers).

Audit Exposure

Another concern is related to the threat of remote state audits. Under the current CSP system, CSPs, not their retailers, are responsible for responding to audit inquiries. In most cases the CSP already has all of the information necessary to respond to such audit requests, without any effort by

the retailer. As this committee considers alternatives to deal with audit concerns, one option is to rely upon the integrity of the states' CSP certification process and shield any retailer relying upon the services of a CSP from remote state audits.

Important Concepts for Alternative Solutions

FedTax believes that the central tenet of any internet sales tax legislation must be a federal framework based upon the current sales tax structure. Anything else would cause an immense disruption to businesses across the nation.

Some witnesses have asserted that SSUTA's simplifications are insufficient to remove perceived compliance burdens. We would note that the other solutions that were proposed, such as origin sourcing or an "IFTA-like" home-base proposal, create compliance burdens of their own—and if they choose these options, states would be jettisoning a fully developed, functioning system that has been eliminating compliance burdens for 15 years in favor of an untested, hypothetical system that might take years to create and that businesses and consumers have no experience using.

Disruption of existing business processes by changing to a new system will damage the economy and cause needless delays in solving this pressing problem.

Compliance burdens can be eliminated by requiring states with collection authority to provide retailers with automated technology solutions (including software and/or services) that can manage compliance tasks for all states with collection authority, and that are verified and certified by each such state's revenue agency to ensure compliance with that state's sales and use tax laws. In addition:

- Certified systems must be allowed to file sales tax returns and remit sales tax proceeds on behalf of remote retailers.
- Certification is necessary for states to have the certainty necessary to grant comprehensive liability relief for remote retailers relying upon such systems.
- States must be required to certify multiple providers to ensure an open and free market.
- Providers of certified systems must be compensated by the certifying state to eliminate costs for remote retailers. Such compensation should be paid by the states from the remotely collected sales tax proceeds.
- Retailers' reimbursement for expenses related to integration and initial setup costs should be paid by the states from the remotely collected sales tax proceeds.
- States must provide publicly available electronic (machine-readable) data sources for sales and use tax rates, jurisdictional boundaries, and taxability of goods and services. These data sources must be available for all businesses to rely upon, even those not using a certified system.
- States must allow certified systems to automatically register businesses in their state.
- States must support a central registration process to allow remote retailers to register easily and quickly in all states.

- States must make a single statewide agency responsible for accepting sales tax returns and sales tax proceeds.
- Recognizing the multichannel nature of modern retail, states must be able to accept multiple (nonduplicative) sales tax returns, possibly one per channel.
- Destination sourcing must be required for interstate sales. Destination-based sourcing returns the tax collected to the customer's tax jurisdiction.
- There must be limitations on audits, such as restricting audits to sellers above a certain threshold, or a consolidated audit, or even exempting retailers that use a Certified Service Providers from audits.

The beauty of this proposal is that this system is in already in place today and it is working. The SSUTA system currently provides proven technology solutions for the thousands of retailers that are already collecting today. Some of the other ideas that have been proposed at the hearing have not been tested and are not currently in use. Forcing states and businesses across the country to adopt radically different systems will create disruption and unnecessary expense.

Why should Congress discard the Streamlined Sales Tax Governing Board, which has been perfected over several years, and replace it with a different structure? A simpler answer would be to give collection authority to all states that meet congressionally mandated minimum simplification requirements and require them to provide technology as listed above to reduce compliance burdens.

We know what works. It is not a single rate. It is not origin sourcing, or any of the other alternatives presented at the hearing. They will simply muddle tax reporting further. Inaction by Congress will encourage states to continue attempts to circumvent *Quill* and find solutions that may or may not benefit the retail community and may or may not further simplification and uniformity.

What won't work:

- Origin sourcing. This scheme shortchanges state and local governments by sending their consumers' tax dollars to other states and countries. It also would turn jurisdictions with no sales tax into e-commerce havens.
- Requiring reporting instead of remittance. This scheme is burdensome for businesses and would require entirely new systems at revenue departments to process and respond to such reports. This is a highly inefficient way to collect tax that is owed.
- Reporting remote sales to a clearinghouse for distribution to states. This increases administrative expenses and replaces one bureaucracy with another—such as creating an IFTA for sales tax.
- Granting states the power to exclude noncompliant retailers rather than having them collect sales tax. States have enough difficulty tracking down in-state sellers that do not collect sales tax; the process of identifying remote sellers that aren't collecting and then engaging in a legal process to bar them from selling into the state, is unduly lengthy and litigious, not to mention very unfriendly to businesses.

Dramatically changing the way sales tax works is not a solution. It would be a disruption for both businesses and governments and carries unacceptable costs for both.

The issues cited as barriers for business to collecting—fear of audits by states where the retailer has no locations, exorbitant integration costs for "free" software, catalog sellers, and data privacy—are all easily resolved by legislation. For example, limitations on the frequency of audits and dollar thresholds can reduce audit burden or risk. Audits of remote sellers could be performed by the seller's home state or by a multistate compact. Legislation should clarify that integration costs should be paid by the states.

CONCLUSION

The simplest, least expensive, and easiest solution is to require remote retailers to collect the sales tax at the destination and provide the technology to do so at no cost.

We urge the committee to draft a bill reflecting these core concepts and report it favorably to the House of Representatives for action in this session of Congress. Your action would reward the years of effort and cooperation between businesses and states to modernize and simplify sales tax collection and administration while eliminating tax compliance burdens.

Mr. Chairman, thank you for the opportunity to submit this Statement for the Record on this important issue.

R. David L. Campbell
Chief Executive Officer
The Federal Tax Authority, LLC

NSGA
NATIONAL SPORTING GOODS ASSOCIATION

Testimony of

Mr. Matthew D. Carlson, President & CEO
National Sporting Goods Association

House Committee on the Judiciary

Hearing on
"Exploring Alternative Solutions on the Internet Sales Tax Issue"

March 12, 2014

1601 Feehanville Drive, Suite 300
Mount Prospect, IL 60056
Tel: (847) 296-6742

Mr. Chairman, Ranking Member Conyers, and Members of the Committee, my name is Matt Carlson, and I appreciate the opportunity to submit this written testimony for the record as the Committee explores ways in which Congress can assist states collect sales and use taxes that are due.

I humbly serve as the President & CEO of the National Sporting Goods Association (NSGA), which represents business owners operating more than 22,000 stores and outlets in all 50 states. NSGA has worked on behalf of sports retailers and dealers since 1929. Our shop owners desperately need decisive action by Congress to return to a level playing field as they compete against the instant discounts Internet-only sellers enjoy by not collecting sales tax as part of online transactions. Main Street merchants across the country are closing their doors in the very communities they have supported for years because they can't compete against an electronic free ride. Close the loophole and make it easy for American merchants to comply.

It is time for this Committee to act in a way that will level the playing field and allow all players in the marketplace to compete by the same set of rules. Our members, many of which sell via the internet, do not fear competition; they fear *unfair* competition, and the current loopholes have the scales tipped in favor of Internet-only sellers who don't collect sales tax. At what point in our history did the federal government choose winners and losers in our American economy? That is exactly what's happening, and it's an injustice.

If members of the Committee believe in preserving American jobs, sustaining local communities, economic self-reliance, and fundamental fairness, then leveling the playing field between brick and mortar stores and Internet-only sellers is imperative. These fundamental values guided our "founding fathers" from the inception of this great nation. Today's democracy stewards should be no different.

Why do we find it acceptable to stand on the sidelines while the Internet-only bully pounds lumps on the brick-and-mortar owners? Many of these owners have invested their lives in building better communities. They pay taxes. They donate time, space and funds to the local schools. They support community fundraisers, and they host local events which bring the community together. Who will do these things when Main Street merchants go away? Who will pay the burden of local taxes formerly paid by those small business owners? Who will occupy the buildings they own or rent? Who will employ the many thousands currently working in those stores? The answer, without a balanced playing field, is "no one."

You have been shown all of the facts and figures regarding the sales taxes that go unpaid thanks to the loophole in the current system. You have heard distortions of the truth by those not wishing to give up their advantage. Many online-only merchants have overstated the burden they might have when obeying states that would require them to collect and remit the sales tax that is due to them. Truth is, the means are there to follow the rules without burdening anyone. Remember, brick and mortar retailers have been complying with these laws all along.

We urge the Committee to expeditiously close this loophole once and for all and find a solution to this issue so that the merchants who are part of our American tapestry don't disappear forever.

Thank you.

Respectfully Submitted,

Matthew D. Carlson
NSGA President & CEO

Statement for the Record

Gregory Scott Humphrey,
Chief Executive Officer, World Floor Covering Association

to the

House Judiciary Committee

March 4, 2014

Chairman Goodlatte, Ranking Member Conyers and Distinguished Members of the Committee, my name is Scott Humphrey. I thank you for this opportunity to provide this written testimony in support of the Marketplace Fairness Act. The Act is of great importance to members of the World Floor Covering Association and is needed to allow for fair competition between the brick and mortar stores and Internet sellers.

I am the Chief Executive Officer of the World Floor Covering Association ("WFCA"), a position I assumed in April 2013. WFCA is a nonprofit national trade association organized under section 501(c)(6) of the Internal Revenue Code. WFCA's members include flooring retailers, commercial contractors, restoration contractors, inspectors and installers. The Association provides information and training to its members and supports other organizations that provide training to entities involved in the flooring industry. WFCA represents its members' interests before Congress, state legislative bodies and federal and state agencies. WFCA also provides its members with information regarding federal and state legislation and agency action. WFCA acts by consensus through a Board of Directors elected by its members, and collects data from its members to develop information regarding legislation and agency matters.

Prior to joining WFCA, I worked for Shaw Industries, a flooring manufacturer. I was at Shaw for 25 years and held a variety of jobs starting with territory sales manager and moving on to a series of jobs overseeing training and development. In 2006, I assumed the responsibilities as Director of Shaw Flooring Network. In that position, I directed over 2,000 independent flooring retailers aligned with Shaw through the Shaw Flooring Network. Through this experience and my work at WFCA, I have developed an understanding of the retail flooring dealer and the many challenges they face.

I submit this written testimony as a representative of WFCA's members. The testimony is based on information provided by members, the data collected by the Association and available statistic.

I. Overview of Retail Flooring Industry

The principal members of the WFCA are entities involved in selling floor covering products and providing or arranging for the installation of floor covering products. Most WFCA members sell a variety of flooring materials, including carpet, natural stone, ceramic flooring and wall tiles, hardwood, laminates, vinyl sheets and tiles, and other resilients such as cork, rubber, linoleum and other plastics. The overwhelming majority of members operate local retail brick and mortar stores. I believe all of the Members of this Committee will find a flooring store in each of their communities.

National statistics indicate that the average retail flooring store is a small business. According to the U.S. Census Bureau, there were 12,883 retail flooring stores in 2010. Revenues for the industry reached $15.47 billion in 2011.[1] Applying those statistics, the average retail store had total sales of $1,200,807 in 2011. According to the Catalina Report as published in Floor Covering Weekly, revenues for floor covering sales reached $18.76 billion in 2012,[2] and is estimated that sales in 2013 were $20 billion.[3] According to The Retail Owner's Institute, the average pre-tax profit margin for retail flooring stores was 3.5% in 2009, -0.7% in 2010, 1% in 2011, 0.8% in 2012 and 2.6% in 2013.[4]

Based on information submitted by approximately 1839 members, WFCA membership fits the national average for retail flooring dealers. Over 78% are small businesses with twenty or fewer employees. About 30% of WFCA members have annual sales of under $1 million, well over half have sales under $2 million a year, and around 80% have sales under $5 million each year. Members report average profits of 1% to 3% depending on the year.

According to the U.S. Census Bureau, retail flooring stores directly hire around 100,000 workers.[5] Based on the information submitted, WFCA members directly employ approximately 32,000 employees and average around 20 employees a store. In addition, around 70% of WFCA members hire independent contractors to install the flooring they sell. A typical installation will involve one to four workers. Accordingly, a brick and mortar store is an important part of its community. It creates local jobs and pays local taxes.

III. Internet Sellers

The Internet is a significant and often positive factor in the American economy. It can provide consumers with product information, expanded options and allow comparative shopping. Most WFCA members have embraced the Internet, developing websites, blogging on new products, advertising and networking. Many retailers allow their customers to order online.

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1 *Id.*

2 Floor Covering Weekly (June 7, 2013) (citing Catalina Group data).

3 Floor Covering Weekly (January 6, 2014) (citing Catalina Group data).

4 The Retail Owner's Institute Benchmark, Pre-Tax Profit Trends, Floor Covering Stores (2014)

5 U.S. Census Bureau, NAICS code 442210 (Floor Covering Stores)(2011).

Accordingly, WFCA and its members support a viable and thriving Internet. They simply want to be allowed to compete fairly with their Internet competitors.

The problem is the inability of states to enforce fully their sales tax laws to include Internet sales. This, in turn, gives the Internet seller an unfair advantage. This is not hypothetical for the flooring industry. Internet sellers actively advertise no sales tax. For example, Ambient Bamboo Floors includes as one of the "Reasons to Choose" them is that there is "No Sales Tax" charged." They specifically claim that:

> The best part about our company is that we do not charge sales tax unless your order is shipped or picked up within Maryland or Arizona. You get a high quality, low cost floor and get to keep the money you would have paid in sales tax![6]

Similarly, iFloor promotes that its customers "[p]ay no sales tax on your flooring purchase when you shop with us."[7] A simple online search will disclose a myriad of similar online ads.[8]

Flooring is a high-ticket item costing thousands of dollars. As result, consumers generally want to see and touch the flooring before purchasing. Increasingly, WFCA retail store members are seeing customers shop the stores, gather information on the flooring, get style numbers and take sample boards home. In many instances, the consumer uses the information gathered to buy the flooring online, using the brick and mortar store as showroom for the Internet sellers. In other cases, when the consumer returns the samples, they insist on the Internet price. The retailer will match the price, but it cannot agree to "no sales tax." By law, the dealer must collect the tax on all sales. The average dealer makes only 1% to 3% profits on a sale; reducing the sales price by the 6% to 10% sales tax would result in a loss. A local dealer simply cannot overcome a "sales tax discount" that usually means hundreds of dollars on a flooring sale.

Internet sales of flooring are increasing rapidly, especially with the introduction of easy to install floors. Today, a consumer can install a wood laminate floor without any glue or nails and Internet sellers are advertising this flooring as "Do It Yourself" installation.[9] Similarly, there are self-adhesive laminates, tiles and vinyl that can be installed by simply peeling off the back sheet and laying the floor tile in place.[10] Shaw and Mohawk, the two largest manufacturers of carpet, sell self-stick carpet tiles, making installation of wall-to-wall carpet easier. There are even systems to allow easy installation of hardwood floors, such as the Elastilon Strong Self Adhesive Hardwood Floor Install System. There are a myriad of other flooring products that a consumer can buy and install him or herself. The problem is not the availability of these products, but that Internet sellers are selling them with no sales tax, creating an unfair and unearned advantage over the local brick and mortar store.

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6 *See* screen shot from Ambient Bamboo Floors' website, attached hereto as Exhibit 1.

7 *See* screen shot from iFloors' website attached hereto as Exhibit 2.

8 *See* other examples of screen shot advertising no sales tax, attached hereto as Exhibit 3.

9 *See* examples of screen shot advertising do it yourself, attached hereto as Exhibit 4

10 *See* examples of screen shot advertising the ease of installation of these products, attached hereto as Exhibit 5

Over the past seven years, there has been a loss of 25% of retail flooring dealers in the United States. While all of this loss is not due to Internet sales, the trend is apparent—the traditional local brick and mortar store on mainstreet cannot survive if Internet sellers are allowed to compete unfairly using no sales tax as an advantage.

IV. The Marketplace Fairness Act

A fundamental aspect of the proposed MFA is to make the existing "Streamlined Sales And Use Tax Agreement" a federally approved program with some additional requirements and safeguards. This agreement requires states to simplify their sales tax requirements by adhering to uniform product definitions, adopting uniform requirements for filing sales tax returns, administering both state and local sales tax collections through a single state office, and allowing retailers to register through a centralized one-stop multi-state registration system. So far 24 states have signed on to and have implemented the necessary legislation to effectuate the Streamlined Sales And Use Tax Agreement.

This program, however, is voluntary and states cannot require Internet sellers to register and collect the taxes. Accordingly, the MFA is needed to allow states to collect the sales taxes that are due on sales to residents in their state. Without the MFA, states will continue to lose significant tax revenues and local businesses will continue to be at an unfair disadvantage in competing with Internet sellers

The MFA would allow states to elect to participate in the program. For a state to use the federal authority to collect sales taxes on Internet and mail order sales it will have to meet the standards for simplifying their sales tax rules and administrative requirements as set forth in the proposed Act. States that voluntarily enter the program and adequately simplify their tax systems should be authorized to collect taxes on sales of goods or services delivered in-state, without regard to the location of the Internet and mail order seller. The Act would require the states to release consumers from tax remittance obligations to participate in the program.

Under the proposed legislation, Internet sellers can elect to register with the "one stop" system covering all participating states or can register directly with each state. To participate a state must also provide the Internet seller free software to implement the collection and remittance of the sales taxes that are already due on these sales.

V. House Judiciary Committee Basic Principles

I have addressed below the "Basic Principles on Internet Sales Tax" set forth by the Committee on September 18, 2013.

1. Tax Relief

Requiring Internet sellers to collect the existing sales tax does not create a new tax. The consumer owes the sales tax on all items he or she purchases whether at a local store or from a remote Internet seller. That is why it is not part of the price, but added to the final price of an item. The problem is there is no practical way to collect the tax unless the seller collects it at the time of the sale. The local retailer is obligated to collect the tax on all of its sales. All the MFA does, and all that WFCA asks, is that state be authorized to require that remote Internet sellers

collect sales tax from its customers just like the local brick and mortar stores now do. Accordingly, the MFA does not create a new tax anymore than enforcing existing tax laws creates a new tax. Rather, it simply creates a practical means of collecting the taxes that are already due.

2. Tech Neutrality

As explained above, the current system does not put brick and mortar on equal footing with exclusively online or brick and click businesses. Brick and mortar stores are at a distinct disadvantage. In essence, out-of-state Internet sellers have "no sales tax discount." As explained above, Internet sellers tout this "discount." Local brick and mortar stores must collect the tax, and that "no sales tax discount" is often the difference between the local stores making or losing a sale. The MFA, therefore, is essential for a fair free market to work in the flooring industry, with all competitors operating under the same rules.

3. No Regulation Without Representation

It is key to note that the seller does not pay the sales tax; it is paid by the consumer. All that the MFA would do is authorize states to require Internet sellers to collect the tax that is due from the consumer. These taxes are determined at the state and local level and are used to support local services and needs, such as fire and police departments, libraries and parks. The consumer, whether he or she buys locally or from a remote Internet seller, lives in the locations where the tax is due and benefits from the services for which these taxes pay. Requiring an Internet seller to collect the tax from these consumers is only fair. The Internet seller does not pay them and the local consumer simply pays his or her fair share.

4. Simplicity

The requirement for out-of-state sellers to collect the sales tax does not impose a significant burden. First, the fundamental aspect of the proposed MFA is to make the existing "Streamlined Sales And Use Tax Agreement" a federally approved program with some additional requirements and safeguards. This program is already working in a number of states.

Second, for a state to use the federal authority to collect sales taxes on Internet sales it will have to meet the standards for simplifying their sales tax rules and administrative requirements as set forth in the Streamlined Sales and Use Tax Agreement as modified by the proposed Act.

Third, the collection is not complicated with today's computer systems. Many brick and mortar stores collect a variety of sales taxes from a variety of jurisdictions, both located within a state and in neighboring states. Simply putting in an address or zip code will allow for the automatic calculation of the amount due. Internet sellers are already savvy with computer systems. They use computers to verify addresses for shipment, to get authorization for credit cards, to target markets and to advertise their product online. A system to correctly calculate a sales tax based on the customer's location takes nothing more than inputting the customer's address. This could not be easier since the Internet seller already has inputted the delivery location at the time of sale.

Fourth, under the MFA, any state that chooses to participate must provide the Internet seller free software to implement the collection and remittance of the sales taxes that are already due on these sales. Moreover, Internet sellers can elect to register with the "one stop" system covering all participating states or can register directly with each state. Accordingly, an Internet seller could elect to deal with a single entity.

Compliance is sufficiently simple to allow any small business to collect sales taxes from their customers. The current MFA establishes a small business exception for any entity with less than $1 million of Internet or mail order sales. This is far too large of an exemption. The average retail store had total sales of $1,200,807 in 2011 and approximately 30% of WFCA members have annual sales of under $1 million. All of brick and mortar flooring retailers collect the sales tax on all of their sales; Internet retailers should be required to do the same.

If the Committee is convinced that the available free computer programs is not sufficient, there is a more sensible alternative to simply exempting every Internet seller with under the $1 million in gross sales. As an alternative, the Act could require that any entity with less than $1 million of Internet sales be obligated to collect only the state sales tax and not any of the local county or city sales taxes for the first two years. Thus these entities would only need to deal with the tax for 45 states and the District of Columbia, hardly an unreasonable burden. The two-year exemption would provide sufficient time for the Internet seller to put into effect the free software offered by the states to collect and remit the sales taxes that are due.

5. States' Rights

State and local governments determine whether to enact, and the amount of, any sales tax. This tax helps support state and local services. The MFA does not require a state to implement a sales tax. To the contrary, the Act leaves it to the states and local jurisdictions to decide whether to implement a sales tax, the amount of the tax, if any, and even whether to participate in the MFA and have remote sellers collect the tax.

Far from imposing a sales tax, the MFA may generate "competition" to provide lower taxes. The state could advertise that it has lower taxes and that these lower taxes apply to all purchases, whether from a local store or an out-of-state seller. In addition, it allows states to collect sales taxes that are already due, freeing each state to determine how to use the taxes. Some state Governors, such as Wisconsin's Gov. Walker and Tennessee's Gov. Haslam, have suggested lowering other taxes. Ohio has already passed a law declaring that passage of the MFA will mean a reduced overall sales tax rate. The MFA embraces state rights by leaving the authority over these issues where they belong—at the state and local level.

6. Privacy Rights

There should be no real privacy issues. Local retailers already collect sales taxes without violating any privacy right of the consumer. Internet sellers' collecting sales taxes would create no new privacy concerns.

VI. Conclusion

The MFA is needed to ensure fair competition, a cornerstone of America capitalism, and to allow states to effectively collect the taxes that are already due on Internet sales to their residents. Without it, local retailers will continue to suffer, local jobs will be lost, tax revenue already owed will not be collected and local communities will suffer.

Testimony submitted to the

United States House of Representatives Committee on the Judiciary

Hearing on:

Exploring Alternative Solutions on the Internet Sales Tax Issue

March 4, 2014

Chairman Goodlatte, Ranking Member Conyers, and members of the committee: thank you for holding a hearing on Exploring Alternative Solutions on the Internet Sales Tax Issue.

I am George Chityat, co-owner of KingWebmaster, LLC, an e-commerce software development company. If you take one thing away from this testimony, please remember that there is no such thing as an easy or cheap software solution for the challenge of remote sales tax collection. It is a false promise.

I built a custom Yahoo cart integration with Avalara sales tax software and so understand as well as anyone the costs of developing connectors between shopping carts and sales tax software solutions. Though my company could profit greatly by the passage of the Marketplace Fairness Act, I am formally opposed it, and any related solution that requires expensive software integration because this legislation would impose great costs on the marketplace and impede entrepreneurship and commerce. I want to tell you about my experience creating software integration solutions with third party sales tax software so that you understand the complexity and scale of cost that a bill such as the Marketplace Fairness Act would impose on businesses.

KingWebmaster developed a "Connector" to integrate Avalara with Yahoo Stores. In order to do so, it not only had to create a system that would connect the two, but it also needed to create an entire system to calculate shipping. The Yahoo Store platform is built in a way that if a 3rd party (in this case Avalara) is providing the sales tax rates, it would also need to provide the shipping rates. The same is true vice-versa - if a 3rd party shipping system is providing shipping rates, it would need to provide sales tax rates.

KingWebmaster spent approximately 150 hours of development and testing time to create the connector between Avalara and Yahoo. However, as for the shipping portion of it, KingWebmaster was already in the business. Since 2006 it has offered a shipping rate service called the Advanced Shipping Manager. This system (or a lighter variation of it) is required in order for the Avalara Connector to work.

KingWebmaster spent over 1,000 hours initially developing its Advanced Shipping Manager as well as countless additional hours over the years maintaining and updating it. The system needed (and still needs) updating on a regular basis just to keep up with UPS, USPS, and FedEx, as they make periodical changes to their systems.

Furthermore, since KingWebmaster's system replaces the existing Yahoo Store shipping system, store owners expect that the company provide at least the same level of functionality with its system that Yahoo offers. Yahoo periodically makes changes to its own system, and KingWebmaster in turn must to do the same.

There are various risks involved with integration. The more servers that are involved in accepting an online sale, the greater the risk of failure. Every one of the servers needs to be up and running for a sale to be completed. Using the Yahoo Store example, adding

KingWebmaster's system with Avalara adds at least two new servers to the equation - KingWebmaster's server, and Avalara's server.

In layman's terms, a server is just a computer like you might have at home or in your office. Computers go down, they need to be restarted, inspected for viruses, and they are also subject to hardware failure. If for example, Avalara's server were to go down, KingWebmaster's system would not be able to obtain the proper tax rate and pass it to Yahoo's server. One of two things would then happen. Either the order would not be able to be completed, or else the sales tax cost would show as $0.00. For the former, the store would lose a sale. For the latter, the store owner would either pay the sales tax from his own pocket, contact the customer for additional payment and risk upsetting the customer and losing the sale, or not pay the tax and risk a penalty.

All of this happens pre-order. However, a lot more needs to be done post-order. KingWebmaster does not do post-order integration. Stores still need to get the proper data into their order management software. They need to know how much money to send to each of the various taxing authorities. They need to know how much tax to calculate when a customer calls to make a change to an existing order. This is yet another integration which require another vendor and incurs greater ongoing costs.

At $200/hr programming time to develop and integrate a TaxCloud or Avalara API with a custom cart costs a minimum of $30,000 just for the connector and at least $200,000 to build the shipping connector that is necessary for the sales tax API to work. $230,000 in initial integration costs for Yahoo to Avalara connector. This is what a business would have to incur on its own if it has built a custom cart.

If a customer uses a 3rd party cart, solutions such as KingWebmaster's for Yahoo would have to be developed. There are over 270 3rd-party carts currently in usage. 35,000 stores use Yahoo's cart. Each of these carts will either have to incur this cost or hope that another developer does so and provides that solution to their customers. There are also countless custom carts in existence that would not even be able to find support, however costly. Ecommerce retailers that use stores/carts that don't have this support will have to build it themselves or else move to a new store platform/cart, which can be a significant expense (as other documentation shows).

If Congress feels that the current physical presence standard needs to be changed, then I would urge you to seek out solutions that would not require the use of third-party software in order to collect and remit sales taxes. Chairman Goodlatte's principles are correct to require that any solution must be both simple to administer and impose no additional burdens on online retailers that are not faced by brick and morter stores. The Senate passed Marketplace Fairness Act is miles away from either requirement.

To continue to believe that mandating the use of software as a solution to the complexity problem would be to fail to understand the realities of the ecommerce landscape or the economic harm such requirements could cause, especially to small and mid-size businesses.

eBay Inc.
2145 Hamilton Avenue
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ebay inc

March 21, 2014

Chairman Bob Goodlatte
Committee on the Judiciary
U.S. House of Representatives
2138 Rayburn H.O.B.
Washington, DC 20515

Ranking Member John Conyers
Committee on the Judiciary
U.S. House of Representatives
2426 Rayburn H.O.B.
Washington, DC 20515

Dear Chairman Goodlatte and Ranking Member Conyers:

eBay Inc. and the hundreds of thousands of small businesses that use our platforms would like to thank you for convening the hearing "Exploring Alternative Solutions on the Internet Sales Tax Issue." On behalf of eBay Inc., I am sharing the following letter and ask that it be placed in the Committee's March 12, 2014, record.

The Marketplace Fairness Act was rushed through the Senate last May without adequate debate, creating great concern among Internet-enabled small businesses that would be negatively impacted by a fundamental change in well-established tax law. eBay Inc. remains committed to working with you, your House Judiciary Committee colleagues and other stakeholders to ensure any solution contains the necessary safeguards so that small businesses, medium-sized enterprises and the largest national retailers all have an opportunity to benefit from Internet and mobile technologies to succeed in the 21st Century retail marketplace and compete locally, nationally and globally.

eBay Inc. would like to commend Chairman Goodlatte for his leadership on this issue. We firmly agree that the seven Internet sales tax principles articulated by the Chairman last fall should serve as the foundation for any Internet sales tax legislation. The principles address many of the concerns shared by the Internet-enabled small business retail community. As the Chairman highlights in the principles, any change in sales tax law should be technology neutral and not create discriminatory compliance or enforcement burdens that offline businesses would not have to comply with. This is a key failing of the Marketplace Fairness Act, which as passed by the Senate would create a disproportionate tax compliance and enforcement burden for Internet-enabled small businesses.

eBay Inc. would like to note that concerns, debate and lobbying activities related to the impact of Internet commerce on the future of retail, as well as on the tax revenues of states and localities, stretch back nearly 15 years. If there was something missing from the excellent debate at the March 12 hearing, it was a discussion on how the changes in the retail markets impact the policy debate. In fact, technology, both the Internet and mobile, has made its way into basically every segment of retail in the United States. Nearly all consumers use the Internet as part of their daily life, and the convergence of mobile technology and the Internet, and devices such as smart phones and tablets, are at the heart of how retail is changing. The way consumers and retail businesses, large, medium-sized and small, use technology as part of their everyday shopping activities is completely different in 2014 than it was in 2000.

While there will inevitably be different views on the best tax policies, we do believe it is important to contribute to a better understanding of the reality of 21st Century retail. There are clear trends in the role of technology that demonstrate how boundaries between on- and offline commerce are blurred, against which policy proposals should be measured. At the heart of this, the Internet has become a part of everyday life and part of the business of nearly every retail business. At the same time, retail over the Internet is only around 7% of total US retail and sales taxes continue to play a similar part of state and local tax policies as they did in 2000. In short, Internet-based retail did not destroy in-store retail and did not end sales taxes as an important component of state and local tax revenue. Against that backdrop, we would like to outline the following important trends.

Discussions on "showrooming" do not reflect trends in retail consumer behavior

An oft-cited reason for needing to "level the playing field" in discussions on online sales tax is that brick and mortar retailers suffer from consumer "showrooming"; that is, where a consumer visits a physical retail store to view, trial or try on an item in order to assist their decision-making about a purchase, before making the purchase from an online retailer because they are able to purchase the item cheaper online (some stakeholders speculate that this may occur because consumers are seeking to avoid the sales tax on certain remote sales). While we do not contend that such examples of showrooming do not happen, we urge members to consider a fuller analysis of consumer behavior trends before deciding whether and how they impact on the sales tax issues at hand.

Analysis from Accenture over the past year contends that "showrooming" is actually less frequent than the opposite trend, which is called "web rooming" in the retail industry. This is where a consumer undertakes their product research online, using tools on retailers' websites that facilitate better comparisons of items, allows them to understand the reasonable price for an item or interact with an item expert to gain the best advice on its use, features or design, identifies where the product is available and for what price, before purchasing the item from a brick-and-mortar retailer. Industry commentators explain that consumers do this because they believe they can get broader and better information online, but wish to use the item immediately, value of option of returning an item they do not end up liking in a store, appreciate the human touch of dealing with a helpful in-store associate, or want to see the item before committing to the purchase. In these cases, it is the online retailers' investment in tailored advice and presentation tools upon which the consumer "free-rides" before making the purchase offline.

The following studies all note the trend that <u>web rooming is more prevalent than showrooming</u>:

- In a February 2014 Accenture study on behaviors over the past twelve months, 78% of consumers said they bought in-store after browsing online, whereas 72% bought online after browsing in a store.[1]
- In the "Accenture Holiday Shopping 2013" report (an online survey of 500 U.S. consumers in September 2013), 65% of online shoppers said they planned to "webroom" that holiday shopping season (up from 56% in 2012). Survey respondents said that avoiding shipping costs (47%) and being able to touch and feel a product before purchase (46%) were their primary motivations for shopping this way. 63% of shoppers said they would showroom. That compares with 56% who said they would do so the previous year, which means "webrooming" is increasing at a slightly faster rate.[2]

[1] *U.S. Seamless Retail Survey Results 2014—Infographic*. 2014. Infographic. AccentureWeb. 20 Mar 2014. <http://www.accenture.com/us-en/Pages/insight-accenture-seamless-retail-survey-2014-infographic.aspx>.

[2] "Holiday Spending Expected to Increase by 11 percent and Nearly all Shoppers Will be Searching for In-Store and Online Discounts and Sales, Accenture Study Finds." *Accenture: News Releases*. Accenture, 7 Oct. 2013. Web. 20

- In its April 2013 "Accenture Seamless Retail Global Customer Study" (an online survey of 6,000 adult consumers in eight countries - United States, U.K., Germany, France, Sweden, Japan, China and Brazil - 750 of which were U.S. consumers, undertaken in November 2012), 73% of respondents indicated that they participated in the practice of "showrooming" in the six months prior to the survey, but an even larger number – 88% – said they participated in "webrooming" in the same period.[3]

In addition to the independent data on this issue, it's worth noting retailer reactions to the instances of showrooming. eMarketer research published in December 2013 concluded that approximately 83% of small businesses acknowledge that "showrooming" either helps their business or has little to no impact.[4] And some of the nation's largest retailers have stated that they have found ways to combat showrooming adequately, or even benefit from web rooming in particular.[5]

Given the greater prevalence of "webrooming", the claim that current sales tax law is driving consumer behavior simply does not make sense. Consumers' web-rooming, which is a perfectly understandable and sensible use of Internet and mobile technology to enhance shopping, shows that consumer use of the Internet is far more complex than just tax policy. Consumers use the Internet to make shopping decisions, and more often than not they choose to make purchases that could be made remotely and without sales tax collection, in a store with sales taxes collected.

Our intention is not to question whether showrooming occurs; rather we wish to point out that it is not a dominant trend and that if other trends are even more prominent, it is very unlikely that the absence of sales tax from some online transactions is a key decision-making element for the majority of consumers in their decision as to where to make a purchase. In short, consumers and retailers use technology and behave in ways that are much more complicated and sensible than this.

The Evolution of Omni-channel Retail

We believe that the repeated reference to "show-rooming" and lack of recognition of "web-rooming" is best understood as simply one manifestation of a fundamental change in retail that has occurred during the 15 years of debate related to sales taxes and Internet commerce. In short, the heart of the debate over Internet sales taxes has been about competition between "store retail" and "Internet retail". But this simply does not reflect the reality of what is commonplace in the retail world – the retail industry itself recognizes that its world is now omni-channel.

What does omni-channel retail mean? It means that the simple view of retail involving store retailers competing with Internet retailers (or catalogue retailers or cable infomercial retailers) is

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Mar 2014. <http://newsroom.accenture.com/news/holiday-spending-expected-to-increase-by-11-percent-and-nearly-all-shoppers-will-be-searching-for-in-store-and-online-discounts-and-sales-accenture-study-finds.htm>.

[3] "Accenture Study Shows U.S. Consumers Want a Seamless Shopping Experience Across Store, Online and Mobile that Many Retailers are Struggling to Deliver." *Accenture: News Releases*. Accenture, 15 Apr 2013. Web. 20 Mar 2014. <http://newsroom.accenture.com/news/accenture-study-shows-us-consumers-want-a-seamless-shopping-experience-across-store-online-and-mobile-that-many-retailers-are-struggling-to-deliver.htm>.

[4] *Impact of Showrooming According to US Small Businesses, Aug 2013*. 2013. Photograph. eMarketerWeb. 20 Mar 2014. <www.emarketer.com>

[5] Fitzgerald, Dres. "Fear of 'Showrooming' Fades." 3 Nov 2013: n. page. Web. 20 Mar. 2014. <http://online.wsj.com/news/articles/SB10001424052702303661404579175690690126298>.

not the world most retailers live in today. This is especially the case for the largest retailers, who have the biggest base of facilities (stores, warehouses and distribution centers) and greatest ability to invest in technology. In short, all larger retailers use Internet and mobile technology to complement their stores. Some use Internet and mobile to drive a distribution-center growth model. But make no mistake, retail is moving in an omni-channel direction, with retailers combining facilities with technology to deal with technology-enabled consumers. The pace of change is fast because consumers are changing their behaviors, the technology tools are changing, and innovators keep innovating. In fact, according to a report from eMarketer, "84% of retailers worldwide said that creating a consistent customer experience across channels was very important."[6] The key take-away is that any sales tax policy change based on the desire to address competition between Internet retailers and store retailers is fundamentally flawed. That might have been retail in 2004, but it is not the case in 2014, and by 2024 it will be a footnote.

While a vision of retail competition between "Internet retail" and "stores" is no longer prevalent, and in short order will border on irrelevant, there is a more lasting competitive framework in which to base tax policy. We believe it is the ongoing competition between large retailers and small retailers. It is critical to note that eBay Inc. serves large, medium and small-sized retailers and entrepreneurs. We provide access to cutting edge Internet and mobile technology services to all size retailers and consumers. We fully understand that all kinds of retailers use all types of Internet and mobile technology. But we also know that large retailers, medium-sized retailers and small businesses are different in key ways. In short, just because a small business with $10 million in annual sales and 15 employees uses the Internet and mobile, and sells to customers in 40 countries, they are nothing like a $100 billion retailer with 150,000 employees who uses the Internet and has customers in 40 countries.

The small business and the giant business both use the Internet, both have facilities, and both sell across the US and around the world. But the 150,000-person retailer has tax, accounting, legal, HR and compliance infrastructure and a network of facilities that probably covers all states and five countries. The small business is run by an entrepreneur, who consults a lawyer when needed and likely has a staff member or local acquaintance help with the books. She has a facility, maybe a shop or a warehouse, and is a vision of 21st Century entrepreneurship. But she's a long way from being a global retailer player who should be expected to ever comply with national and global tax collection in the same manner as the multi-billion-dollar retailer.

It should also be noted that the small business retail entrepreneur and the giant retailer are similar in that they both use software for their tax compliance. But once again, that does not make them the same. The giant retailer understands that good software is not enough to handle national-scale tax compliance and enforcement, and they have teams of accountants and lawyers to deal with tax agencies and audits. The small business owner does not have those teams.

The need to protect Internet-enabled small retailers against disproportionate burdens

eBay Inc. supports the development of a retail market that enables retailers of all sizes to thrive. Competition should be about developing the best business model and the provision of the most compelling omni-channel services to consumers. eBay Inc. is proud to support large and small retailers through its Internet and mobile platforms and technologies.

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[6] eMarketer Inc. 18 Dec 2013. *Retailers Lag Behind Consumers' Omnichannel Desires.* eMarketer Inc.

As a company that has proven to serve as a platform for small business retailers and a tool to encourage small business development and entrepreneurship, we are especially sensitive to measures that would especially impact smaller businesses. This is the reason that our position in the online sales tax discussions is focused on the need to protect those businesses from disproportionate burdens. With consumers now seeing the retail markets as omni-channel (that is, they use on- and offline channels interchangeably) for almost all goods, we believe that these burdens need to be assessed in the context of big retailers and small retailers, not online retailers and offline retailers, because the latter distinction is increasingly blurred and cannot be the basis of forward-looking legislative proposals.

Testimony for the March 12 House Judiciary Committee hearing has already outlined the compliance burden facing small businesses from a mechanism such as the Senate-passed Marketplace Fairness Act. NetChoice's excellent statements contained the following passage:

> *The most significant reason that MFA fails all seven of the Principles is that it would force catalog and Internet sellers to incur significant new tax compliance costs that are not borne by brick-and-mortar retailers. Instead of leveling the playing field, MFA would heavily discriminate against e-commerce. Under MFA, brick-and-mortar stores would not have to comply with out-of-state tax rules where they have no physical presence, but e-commerce stores would. Moreover, because these costs are disproportionately expensive for small businesses, the small e-commerce firms would be hardest hit.*
>
> *The SSTP's own Cost of Collection[7] study found that the smallest businesses spend 17 cents for every tax dollar they collect for states. That is vastly more than their large-scale competitors. Even if the "free" tax software were to work as advertised (and as explained later, it will not), that would help eliminate only two cents of the extra costs. So a small business with annual revenues of $1 million would still incur a new cost burden equal to 15 cents on every dollar it collects, for tasks such as:*
>
> - *Computer consultants to integrate new tax software into their home-grown or customized systems for point-of-sale, web shopping cart, fulfillment, and accounting*
> - *Training customer support and back-office staff*
> - *Answering customer questions about entity and use exemptions and sales tax holidays*
> - *Responding to audit demands from 46 states – plus up to 550 Indian Tribes, per S.743*
> - *Accountants and IT consultants to help with all of the above*
>
> *These collection burdens will impose impossibly high costs on small catalog and online businesses. Ask any small business – a brick-and-mortar store on Main Street, or an online store – and you'll hear it's hard enough to collect sales tax for one state. It would be a nightmare for a small business to have to comply with the rules of all 46 states, each with sales tax rates, regulations, and unique filing burdens of its own.*

[7] National Economic Consulting, "Retail Sales Tax Compliance Costs: A National Estimate, Volume 1." PriceWaterhouseCoopers, 7 Apr 2016. Web. 20 Mar 2014. <http://netchoice.org/wp-content/uploads/cost-of-collection-study-sstp.pdf>.

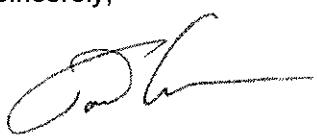
Indeed, one of the most important takeaways from the March 12 hearing was the clear sense that members of the committee recognized that burdens associated with the Senate-passed Marketplace Fairness Act cannot be solved simply through the use of sales tax software.

Next Steps for the Committee

As stated above, eBay Inc. urges members to adhere to Chairman Goodlatte's principles for any legislation on the issue of state and local sales tax collection. As we have clarified repeatedly during discussions over many years, eBay Inc.'s primary concern is that small retailers using online channels, whether they are exclusively online retailers or retailers that use both physical and online channels, not be penalized for innovating and using Internet and mobile technology in the same manner as the largest national retailers.

We noted above that we were pleased to hear these concerns reiterated by most of the committee members at the March 12 hearing. Whichever path the committee members now choose, eBay Inc. implores you to use a combination of protections for small businesses to achieve this purpose. eBay Inc. reiterates its belief that a robust small business exemption is an appropriate method to address that concern, and as participants in the House Judiciary Committee hearing noted, further consideration should be given to specific measures to counter certain burdens. For all these matters, eBay Inc. remains a committed participant in this process and will continue to give a voice to the small businesses that stand to be impacted most by the outcome of this discussion.

Sincerely,



Tod Cohen

Vice President & Deputy General Counsel, Global Government Relations
eBay Inc.

Testimony submitted to the

United States House of Representatives Committee on the Judiciary

Hearing on:

Exploring Alternative Solutions on the Internet Sales Tax Issue

March 4, 2014

Chairman Goodlatte, Ranking Member Conyers, and members of the committee: thank you for holding a hearing on Exploring Alternative Solutions on the Internet Sales Tax Issue.

My name is McKane Davis. I'm the President of Scrapbook.com and co-founder of the eMainStreet Alliance. Scrapbook.com is a small family business, and we sell craft supplies through our website and other channels online. I personally oversee all technology for our business. I am intimately familiar with software integrations and how they will affect my business and other businesses.

Just before the Marketplace Fairness Act was passed in the Senate, I started exploring the costs to integrate the software into our systems and I got very concerned very quickly. Even though the bill said "free software" from Certified Software Providers (CSPs) would be provided by the states, I bid out the costs to integrate the software with our systems and discovered that in order to be compliant with the Senate's version of the Marketplace Fairness Act, my business would have to spend approximately $60,000 dollars in the first year alone in integration costs.

That expense is a grave threat to my business. I can tell you unequivocally, the notion of free sales tax software is a myth and any solution that Congress pursues ought to be so simple that any business - online or off - could collect and remit the tax without the need for additional software. Software is not a panacea, especially government mandated software. The healthcare.gov website is a very good example of what can happen when government mandated software does not work. If software is required, Congress should ensure that the states *compensate remote sellers for the expenses that they incur to become cross-state tax collectors.*

As I looked at the effects of Marketplace Fairness Act on my business I also discovered that we would be responsible to categorize all of our products to ensure that we are not charging sales taxes for exempt products or neglecting to charge on taxable products. Under the MFA there would be no standard categorization structure for tax-exempt products and frankly, it's a mess.

We currently carry over 40,000 products and we add about 2,000 new products every month. Most of our products are very small and inexpensive. We sell buttons, stickers, beads, scissors and other craft supplies. Our products can sometimes be used to make clothes depending on the customers' intention and application of the products. In some states, buttons that are used on clothes are tax exempt, but decorative buttons that are used on cards or home decor, for example, are not. Scissors that are used to cut fabric for clothes are tax exempt, but scissors that are used to cut paper are not. But what about scissors that are classified as generic scissors or "all-purpose" but can be used for cutting both fabric and paper? I still don't have a clear answer.

Where answers to confusing categorization questions do exist they are usually found in the case law and are impossible to find, and where the answers do not exist, the ultimate decisions are left to auditors or the courts. Even if we could know how to categorize all of our products correctly, we would have to manually categorize over 40,000 products differently for every

channel we sell through (once for our own site, once for eBay, once for Amazon, etc.). We would have to hire a dedicated, skilled employee to research and categorize all of our existing products and then we would keep paying them in perpetuity for all of our new products that we add every month. We do not have the resources to absorb this cost. This is an unfair burden that would be placed on my business and other small businesses. *I feel it is imperative that any solution proposed by Congress must mandate that the states adopt a standard categorization structure for all channels and it must be drastically simplified. And in the absence of a homogeneous categorization structure, Congress should mandate that the states compensate remote sellers for the costs of categorization.*

While all of Chairman Goodlatte's principles make good sense, two are particularly relevant here and must be embraced by the committee as it moves forward.

1) Tech Neutrality – The tax compliance burden on online sellers should not be less, but neither should it be greater than for similarly situated offline businesses.
2) Simplicity – The law should be so simple and compliance so inexpensive and reliable as to render a small business exemption unnecessary.

As I discovered just how disruptive and expensive the MFA would be for my business, I reached out to other small ecommerce businesses and quickly discovered that our costs were not an outlier. In fact, many other small business owners had done the same analysis independently and their costs were also extremely high.

Justin Krauss from GarageFlooringLLC.com is a small business owner in Colorado that does cash sales to consumers in remote states. The bids for software integration and set-up for his business came to $70,000. If a bill like the MFA that requires sales tax software integration were to pass, he'd also have to pay to upgrade his Sage Accounting system to enterprise level because the version he has isn't compatible with the CSP software. This is a very large expense. Backward compatibility issues are very serious and sometimes cannot be resolved without huge investments in time and capital.

Peter Ollodart, a former director level product manager at Microsoft, was in charge of ISV compatibility programs for Windows 2000. In 2012, he bought Puget Sound Instrument which does a significant portion of business online. Peter explored the costs of complying with the Senate's version of the MFA and found that it would be about $30,000 in the first year alone, and none of the sales tax software providers offer a solution that is compatible with his accounting system on SCO Unix. If the MFA were to pass he would be compelled to move from his current accounting system and that transition will cost an additional $40,000. The cost of integration and re-platforming would result in significant losses for Puget Sound Instruments and likely force Peter to shut down the online portion of his business. Peter knows firsthand that the MFA would cause huge backward compatibility issues and he has publicly stated that he believes that the Software Vendors are understating the enormity and complexity of integration, compatibility testing and labor costs to comply with any legislation that forces sales tax software integrations.

These are just a few of literally hundreds of examples from small business owners who I have spoken with. We are all very concerned because we would incur onerous integration costs (in addition to exponentially increased audit risk).

I think it is important to consider that Internet retail is a very low-margin business. There is a lot of downward pressure on pricing because all of our competitors are just a click away. Consider that even Amazon.com has a 1% net profit margin - a margin not uncommon in the ecommerce space. A business doing $1M in gross sales at Amazon's margins will only have about $10,000 in profit left over at the end of the year. In fact, my own business has had years where we have lost money or just broke even. For many online businesses the mandated costs alone can and will wipe out their entire annual profit, or even put them out of business. I believe any law that could drive any company out of business just by making them tax collectors for remote states should be a non-starter in Congress.

I see the wisdom in Chairman Goodlatte's guidelines as they provide necessary protections for online businesses and restore sanity to a conversation that has, unfortunately, been dominated by special interests that appear to be unsympathetic to the economic realities of small and mid-size businesses.

I believe that the current physical presence standard satisfies all of Chairman Goodlatte's principles. That said, if Congress feels the need to compel remote businesses to become tax-collectors for states in which they do not reside, then it is imperative that Congress be disciplined in its approach and find a solution that does not require government-mandated software integrations and does not introduce a small business exemption. The states do not have size-based collection exemptions for any businesses in their home states and federal legislation should preserve this practice and follow suit. Any exemption is fundamentally unfair and would introduce disincentives for businesses to grow past the threshold. Any bill that would entertain an exemption is one that starts with an admission that said legislation is fundamentally flawed.

The Real Estate Roundtable

Hearing on Exploring Alternative Solutions on the Internet Sales Tax Issue

House Committee on the Judiciary

Statement for the Record

Submitted by Jeffrey D. DeBoer
President and Chief Executive Officer
The Real Estate Roundtable

March 12, 2014

The Real Estate Roundtable is pleased for the opportunity to submit a statement for the record in conjunction with the House Committee on the Judiciary's hearing on *Exploring Alternative Solutions on the Internet Sales Tax Issue.*

The Roundtable brings together leaders of the nation's top publicly-held and privately-owned real estate ownership, development, lending and management firms and leaders of major national real estate trade associations to jointly address key national policy issues relating to real estate and the overall economy. Collectively, Roundtable members' portfolios contain over 5 billion square feet of office, retail and industrial properties valued at more than $1 trillion; over 1.5 million apartment units; and in excess of 1.3 million hotel rooms. Participating trade associations represent more than 1.5 million people involved in virtually every aspect of the real estate business.

The Marketplace Fairness Act is important to The Real Estate Roundtable, and the commercial real estate industry as a whole, for a multitude of reasons. First, our members own and operate many of the shopping centers and physical marketplaces where retail activity occurs and thus have a strong direct interest in the health and vibrancy of America's retail sector. Second and more broadly, through their property and income tax contributions, commercial real estate owners of all types finance a significant share of the public services provided by state and local governments. Taxes derived from real estate ownership and transfer represent the largest source — in some cases approximately 70 percent — of local tax revenues, helping to pay for schools, roads, law enforcement and other essential public services. As one of the largest sources of state and local tax revenue, commercial property owners, investors, and developers have a significant interest in ensuring that state and local tax systems work fairly and efficiently. Third and most importantly, the strength and prosperity of commercial real estate is closely aligned with the well-being of local communities and working Americans. Tax policies that promote and sustain broad-based job and income growth are the economic foundation that supports our ability to continue investing in capital-intensive, productive real estate assets.

The Real Estate Roundtable has long advocated for pro-growth tax and regulatory policies that are simple, predictable, and consistent. In the context of tax reform, the Roundtable has argued that the tax system should not favor certain types of economic activity or investment over others. Rather, federal laws should encourage job-creating capital investment without picking winners and losers in the marketplace.

Unfortunately, with respect to retail activity, existing federal law has had the opposite effect. The failure of Congress to enact legislation authorizing States to collect sales tax on transactions involving remote sellers means that the owners of physical stores operate at a significant and unfair competitive disadvantage relative to online retailers. The discriminatory taxation of "brick and mortar" retailers vis-à-vis internet-based sellers distorts the marketplace by preventing businesses across the country from competing with one another on a level playing field, on the merits.

In the same way that tariffs disrupt free trade and the efficient allocation of capital across borders, prohibiting States from uniformly applying sales tax collection requirements on commercial transactions rewards certain economic actors over others and prevents free and fair competition. As a result, according to the nonpartisan Congressional Budget Office (CBO), the current system reduces national income.[1] A study by CBO concluded that "[r]emote-seller collection of use taxes would eliminate the uneven taxation of identical goods purchased from a local seller and a remote seller and thereby reduce the loss of national income that results when such tax differentials cause people to make purely tax-motivated decisions about consumption and production."[2] State and federal tax policies should not result in two separate tiers of taxation that impose a higher burden solely on the basis of the medium in which a retail transaction occurs.

Moreover, rather than reducing the burden on taxpayers, Congressional inaction has resulted in higher taxes on the smaller, remaining state and local tax base. Because States are unable to apply sales taxes fairly and proportionately across the full landscape of retail activity, they are inevitably forced to raise income taxes, property taxes, and the applicable sales tax rate on remaining taxable transactions to fill the hole in the tax base. Between 1997 and 2010, sales tax revenue fell from 35.9 percent of total tax revenue for state and local governments to 34 percent. At the same time, property tax revenue as a percentage of tax revenue increased from

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[1] Congressional Budget Office, *Economic Issues in Taxing Internet and Mail-Order Sales*, at vii (Oct. 2003). According to CBO:

> Consumers may be willing to purchase a good remotely even if the total cost of production and delivery exceeds the comparable instate cost because the money they save in taxes compensates them for the money they pay in shipping costs. Similarly, producers may be willing to construct facilities in locations where production and shipping costs are high to avoid nexus and the need to charge their customers sales taxes. The more unevenly a tax is applied, the more producers and consumers waste resources in efforts to avoid it—thereby reducing economic efficiency.

[2] *Id.*

30 percent to 34.6 percent.[3] These trends will only worsen as the share of retail activity conducted over the internet continues to climb.

If the hope or expectation is that prohibiting States from collecting taxes on internet transactions will lead to a smaller overall tax burden, the evidence suggests otherwise. On the contrary, the current regime is shifting the composition of state and local tax revenue (the "tax mix") in a direction that will ultimately reduce long-term economic growth. The inability of States to tax online transactions is leading States to raise taxes on savings (in the form of property taxes) and labor (in the form of income taxes) that are even more socially and economically detrimental than taxes on consumption. Between 1997 and 2011, total state and local sales tax revenue increased 76 percent. In contrast, total state and local income tax revenue increased 79 percent and property tax revenue increased 102 percent.[4]

Ironically, the net effect is the exact opposite of the overarching goal embraced by Members of Congress as they pursue fundamental tax reform – the desire to achieve stronger economic growth through smart tax reforms that broaden the tax base and lower marginal tax rates. At the state and local level, the failure to pass the Marketplace Fairness Act is leading to higher tax rates, a smaller tax base, and an anti-growth "tax mix" that encourages States to adopt even greater taxes on savings and work.

The Marketplace Fairness Act would address the underlying problem with a balanced approach that allows States to reduce tax rates by broadening the tax base.[5] At the same time, the legislation would take aggressive steps to minimize the compliance burden created by the new tax collection responsibilities. The status quo is distorting economic behavior, and as a result, reducing national income. The situation is not self-rectifying; it will only get worse with time as more and more economic activity migrates to the internet. In the time remaining in the 113th Congress, we encourage your Committee to move forward with legislation that would strengthen the economy and boost job growth by removing the legal constraints that stand in the way of a fair and level playing field for retail activity.

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[3] The Urban Institute-Brookings Institution Tax Policy Center, State and Local Government Finance Data Query System, available at: http://slfdqs.taxpolicycenter.org/pages.cfm. The data is drawn from the U.S. Census Bureau, Annual Survey of State and Local Government Finances, Government Finances, Vol. 4, and Census of Governments (1977-2011).

[4] *Id.*

[5] In the State of Florida, for example, the current governor has indicated he only would use the authority to impose sales tax collection requirements on remote sellers as a means to lower the tax burden on businesses that operate locally, not as a means to raise total tax revenue. *See* Gray Rohrer, *Gov. Scott Says He Would Sign Internet Sales Tax Bill, with Caveat*, THE FLORIDA CURRENT (Dec. 21, 2011), *available at*: http://goo.gl/Brs8RM.

ATTORNEY GENERAL
STATE OF MONTANA

Tim Fox
Attorney General

Department of Justice
215 North Sanders
PO Box 201401
Helena, MT 59620-1401

March 12, 2014

Hon. Bob Goodlatte
Chairman, House Judiciary Committee
Hon. John Conyers, Jr.
Ranking Member, House Judiciary Committee
2138 Rayburn House Office Building
Washington, D.C. 20515

Chairman Goodlatte and Ranking Member Conyers:

Thank you for the opportunity to provide the U.S. House Judiciary Committee written testimony for its "Exploring Alternative Solutions on the Internet Sales Tax Issue" hearing. I hope to express some of my overall concerns with federal legislation on state sales tax issues.

Since early 2013 when I was first elected to office, I have followed the progress of the "Markplace Fairness Act" (S. 336/S.743/H.R.684). The legal concerns I saw in the Act led me to form a multi-state, bi-partisan coalition of attorneys general who share those same concerns. To date, General Rosenblum (D-Oregon), General Geraghty (R-Alaska) and General Foster (D-New Hampshire) have joined this coalition. Last summer, this group sent a letter to every member of the U.S. House detailing the constitutional problems in the bill. This written testimony summarizes the contents of that letter.

By authorizing the enforcement of state sales tax laws that require remote sales retailers to collect and remit tax proceeds to out-of-state taxing authorities that the retailer has not established "minimum contacts" with, the Act violates the Due Process Clause. Although Congress can authorize the enforcement of state legislation that burdens interstate commerce, Congress may not authorize the enforcement of state laws that violate the Due Process Clause. So, although this Act may clear the Commerce Clause hurdle, state taxing authorities wishing to collect sales taxes from out-of-state businesses will still face a Due Process Clause hurdle.

The Due Process Clause "demands that there be some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax, as well as a

rational relationship between the tax and the values connected with the taxing State."[1] For purposes of evaluating whether this type of law violates the Due Process Clause, the relevant inquiry is not whether the remote sales business has a "physical presence" in the taxing state, but whether the business has adequate contacts with the taxing state "such that maintenance of the suit does not offend traditional notions of fair play and substantial justice."[2]

Under this standard, an out-of-state retailer that purposefully avails itself of the benefits of an economic market in the forum state by engaging in continuous and widespread solicitation of business will have established minimum contacts with the forum state sufficient to satisfy Due Process. This Act, however, does not limit the enforcement of state sales taxes to remote sales retailers that have purposefully availed itself of benefits in the taxing forum. Instead, it will authorize enforcement of state sales tax laws that require any remote sales retailer located within our borders with a website and a single customer in a distant location to collect and remit taxes from that transaction. Under the Act, it makes no difference whether or not the retailer targeted the taxing forum or had a physical presence there. As a result, any state's efforts to enforce the collection of sales tax proceeds from remote sales retailers with little or no contact with the taxing authority will remain constitutionally suspect. This uncertainty will trigger years of costly litigation for state taxing authorities and remote sales retailers as the courts define the contours of what constitutes adequate contact to satisfy Due Process.

Aside from the costly Due Process litigation this Act will trigger, requiring small, brick-and-click remote sales retailers to collect and remit sales taxes to upwards of 9,600 taxing jurisdictions will be a costly burden on our small businesses making it more difficult for them to compete in the market. Given the clear legal and economic pitfalls the Act presents, I strongly urge you to oppose it.

In terms of alternatives to the Act, I would continue to urge caution. I understand many states are struggling to collect revenues they feel are due to their coffers from internet transactions, but some states have also chosen not to enact general sales taxes at all. A federal fix for some states' revenue problems becomes a new problem for states like Montana that have consistently rejected a general sales tax. Burdening small business owners in Montana with the tax collection duties for thousands of other taxing jurisdictions is a federal mandate that does nothing to create good-paying jobs and strengthen the economy. Not to mention,

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1 *MeadWestvaco Corp. v. Illinois Dep't of Revenue*, 128 S Ct. 1498, 1505 (2008) (internal quotations omitted).

2 *Quill v. North Dakota*, 504 U.S. 298 (1992) (quoting *Int'l Shoe Co. v. Washington*, 326 U.S. 310, 316 (1945)).

many likely proposed alternatives to the state sales tax level will continue to run into the Due Process Clause hurdles I have detailed earlier when approached from a one-size-fits-all federal solution.

Furthermore, it is incongruous with principles of good government and fiscal conservatism to encourage the tax-and-spend propensities of many states and localities, particularly those that are in debt, by allowing them to tax non-residents over the internet. Congress should refuse to be the tax "pusher" for these tax-and-spend "junkies." As one of the few states with both a state constitution balanced-budget requirement, and a balanced budget, Montana objects to Congress placing any further burdens on our job creators and hard-working citizens.

I urge your committee to reject the so-called "Marketplace Fairness Act" and the idea of a federal fix on the state sales tax issue. Montana's job creators are trying to figure out how to put more people to work, enhance markets and create profit – not solve the revenue problems of other states. Thank you for your consideration of this testimony.

Sincerely,

Timothy C. Fox
Attorney General of Montana

Statement for the Record

Kelby Frederick
Co-CEO/Owner, My Flooring Texas, LLC

to the

House Judiciary Committee

March 4, 2014

Chairman Goodlatte, Ranking Member Conyers and Distinguished Members of the Committee, my name is Kelby Frederick. I thank you for this opportunity to provide this written testimony in support of the Marketplace Fairness Act ("MFA"). The Act is of great importance to me as an owner and operator of a brick and mortar retail business and is crucial to allow me to compete fairly with Internet sellers.

I am the Co-CEO and co-own with Scott Steel My Flooring America Texas, which operates nine brick and mortar stores. We have three retail stores in Houston and two in Dallas operating under the name My Flooring America. These locations are full service brick and mortar stores offering all types of floor coverings at retail. In addition, we own and operate four brick and mortar ProSource stores in Houston, which offer a full line of flooring and kitchen and bath material supplier to the building trade. We also operate Xpress Floors: a shop at home retail flooring business in the Dallas Fort Worth area that uses My Flooring America's distribution center in Denton, Texas.

The business was started 1972 and Mr. Steel and I are second generation owners. Our stores have 85 employees. In addition, on any given day, we engage 25 independent contractor installation crews consisting of 2-3 people per crew installing the flooring the company sold.

I submit this written testimony to explain the need for the Marketplace Fairness Act. My testimony is based on personal experience as a local brick and mortar retailer.

I. Unfair Competition by Internet Sellers

The Internet is a significant innovation that we ourselves have embraced. We have websites for my stores, we blog on new products, we advertise online and we use social networking to promote our business. Far from wanting to inhibit the Internet, we only want a fair marketplace were our Internet competitors operate under the same rules that we brick and mortar stores do,

The problem is the inability to of states like Texas to enforce fully their sales tax laws to include Internet sales. This, in turn, gives the Internet seller an unfair advantage. This is not hypothetical for the flooring industry. Internet sellers actively advertise no sales tax. Our company markets both its retail and wholesale divisions as a "Price Match Guarantee." Increasingly, customers are bring in quotes from Internet sellers at artificially lower prices based in part on these sellers claiming that the customer will save the sales tax. Inasmuch as the industry's net profit margin is between 2% to 4%, the 8.25% sales tax often exceeds our profit margin. We are forced to either match the bottom line price whereby we lose money or lose the sale. Since approximately 50% of our company's sales are derived from repeat and referral business, we are often forced to absorb the amount of the tax in order to match the Internet price. Our company simply cannot risk having that customer not come back or communicate to his or her acquaintances that the company's products are "over-priced". We also cannot continue to operate where we lose money on sales.

The net result is that companies like ours is at a substantial disadvantage due to the fact that the Internet companies are not collecting the sales tax we are required to collect. Since flooring is a large-ticket item, the tax can be a substantial amount. I firmly believe in limited taxation and do not wish to support any sort of tax increase. However, it is only fair to hold a company that sells the exact same items, sourced from the exact same suppliers, selling to the exact same consumers, in the exact same location, to the exact same taxation standard. The current system discriminates against the local brick and mortar store and threatens to destroy the small businesses that are the backbone of the American economy.

Internet sales of flooring are increasing rapidly, especially with the introduction of easily to install floors. Today, a consumer can install a laminate floor without any glue or nails. For example, Armstrong makes a laminate floor that simply snaps together. Similarly, there are self-adhesive laminates, tiles and vinyl that can be installed by simply peeling off the back sheet and laying the floor tile in place. Carpet manufacturers are selling self-stick carpet tiles, making installation of wall-to-wall carpet easier. There are a myriad of other flooring products that a consumer can buy and install him or herself. The problem is not the availability of these products. We promote and sell them too. The problem lies in the fact that Internet sellers are selling them with no sales tax, creating an unfair and unearned advantage over local brick and mortar stores.

Since state cannot alone fix this problem, the only sensible solution to this problem is the MFA. The Act leaves it to the states, where it belongs, to determine its sales tax application. The MFA authorizes, but does not require, a state to have Internet sellers collect the sales tax just like local retailers do now. Sales taxes are set at the state level to provide for local services and needs. These taxes pay for fire and police departments, libraries, parks and a host of other local projects and services. The local residents buying online benefit from those services and projects, but do not pay their fair share. The loss of the sales tax on Internet sales can only lead to higher taxes to support these local needs.

II. House Judiciary Committee Basic Principles

I have addressed below the "Basic Principles on Internet Sales Tax" set forth by the Committee on September 18, 2013.

1. Tax Relief

Requiring Internet sellers to collect the existing sales tax does not create a new tax. The consumer owes the sales the tax on all items he or she purchases, whether at a local store or from a remote Internet seller. The problem is there is no practical way to collect the tax unless the seller collects it at the time of the sale. The local retailer is obligated to collect the tax on all of its sales. All the MFA does is allow states to also require that Internet sellers collect sales tax from its customers. The MFA simply creates a practical means of collecting taxes that are already due. The Act does not create a new tax anymore than any law that allows for the enforcement of existing tax laws creates a new tax.

2. Tech Neutrality

Internet sellers are selling products with no sales tax, creating an unfair and unearned advantage over local brick and mortar stores. These out-of-state Internet sellers advertise a "no sales tax" discount. Local brick and mortar stores must collect the tax, and that discount is often the difference between the local stores making or losing a sale. The MFA supports the free market economy where everyone has a fair chance to compete under the same rules. Under the current situation, local stores are not on equal footing with their online competitors.

3. No Regulation Without Representation

The party paying the tax, the consumer, lives in the community were he or she elects the local officials who determine whether to have a sales tax, the amount of the tax and how to spend those tax dollars. These taxes are used to support local services and needs, such as fire and police departments, libraries and parks. The consumer, whether he or she buys locally or from a remote Internet seller, lives in the locations where the tax is due and benefits from the services for which these taxes pay. The Internet seller does not pay the sales tax. Rather, all that the MFA would do is authorize states to require Internet sellers to collect the tax so that the local consumer simply pays his or her fair share.

4. Simplicity

The requirement for out-of-state sellers to collect the sales tax does not impose a significant burden. The collection is not complicated with today's computer system. In Texas, businesses can remit sales tax via the Internet with a computer and modem. Accordingly, an Internet seller, who is already savvy with computer systems, should have no problems. Internet sellers already use computers to verify addresses for delivery, get authorization for credit cards, and advertise their product online. To calculate the correct sales tax takes nothing more then inputting the customer's address. This could not be easier since the Internet seller already inputs the delivery location at the time of sale.

Moreover, the MFA would require a state to meet the standards for simplifying their sales tax rules, provide the Internet seller free software to implement the collection and remittance of the sales taxes that are already due on these sales, and allow Internet sellers to elect to register with the "one stop" system covering all participating states. Accordingly, it costs nothing, is easy to use and uses the information the Internet seller already collected, the consumer's address.

Compliance is sufficiently simple so a small business exception is not needed. The current MFA establishes a small business exception for any entity with less than $1 million of Internet or mail order sales. This is far too large of an exemption. A $1 million is approximately the size of the gross sales of the average retail flooring dealer in the United States. There simply is no need for a small business exception.

5. States' Rights

It is key to recognize that state and local governments determine whether to have a sales tax, the amount of the tax, and how to speed those funds. These taxes support the state and local services and projects. The MFA does not require a state to implement a sales tax. To the contrary, the Act leaves the states and local jurisdictions to decide whether to implement a sales tax, the amount of the tax, if any, and even whether to participate the MFA and have remote sellers collect the tax. The important factor is that all sales taxes are local and that the very elected officials who decide sales tax issues are directly responsible to their constituents. The MFA does not create a national tax, but simply allows states to enforce the tax fairly to all purchases. If a state's voters do not want sales taxes collected on Internet sales, the state can decide not to take advantage of the authority in the MFA to collect the tax from online sellers.

6. Privacy Rights

There should be no privacy issues. As a local retailer, I already collect sales taxes without violating any privacy right of my consumer. Internet sellers' collecting sales taxes would create no new privacy concerns.

III. Conclusion

The MFA is needed to ensure fair competition, a cornerstone of the America capitalism, and to allow states to effectively collect the taxes that are already due on Internet sales. Without it, local retailers like me will continue to suffer, local jobs will be lost, tax revenue already owed will not be collected and local communities will suffer. The MFA offers a fair solution without imposing unfair burdens on the Internet seller. To the contrary, the Act will allow a level playing field for all competitors, whether a brick and mortar store, exclusively an online retailer or a brick and click business.

Attachment 1

Store Locations

My Flooring America
3008 S. I-35 East
Denton, TX 76210
Size 15,000 sq ft
Texas 26th District: Rep. Michael Burgess

My Flooring America
3001 Long Prairie Road
Flower Mound, TX 75022
Size 8,500 sq ft
Texas 26th District: Rep. Michael Burgess

My Flooring America
22121 Katy Freeway
Katy, TX 77493
Texas 10th District: Rep. Michael McCaul
Size 5,000 sq ft

My Flooring America
3337 Highway 6
Sugar Land, TX 77478
Size 7,000 sq ft
Texas 22nd District: Rep. Pete Olson

My Flooring America (and corporate HQ)
16800 Texas Ave.
Webster, TX 77598
Size 16,000 sq ft
Texas 22nd District: Rep. Pete Olson

ProSource of The Woodlands
503 Spring Hill Dr
Spring, TX 77386
16,000 sq ft
Texas 8th District: Rep. Kevin Brady

ProSource of Clearlake
16900 N. Texas Ave
Webster, TX 77598
17,000 sq ft
Texas 22nd District: Rep. Pete Olson

ProSource of NW Houston
9009 Pinehill Ste 200
Houston, TX 77478
13,000 sq ft
Texas 18th District: Rep. Sheila Jackson Lee

ProSource of Sugar Land
12300 Dairy Ashford Ste 200
Sugar Land, TX 77478
12,000 sq ft
Texas 22nd District: Rep. Pete Olson

Lewis, Ashley (Judiciary)

From: Huff, Daniel
Sent: Thursday, March 27, 2014 12:33 PM
To: Lewis, Ashley (Judiciary)
Subject: Emailing: WFCA Melissa Murphy Testimony.pdf, WFCA Phil Koufidakis Testimony.pdf, WFCA Roger Wilson Testimony.pdf, WFCA Scott Appel Testimony.pdf, Written Testimony from General Fox Regarding Alternatives to the Markplace Fairness Act.pdf, 72 TNI 49 .pdf,
Attachments: WFCA Melissa Murphy Testimony.pdf; WFCA Phil Koufidakis Testimony.pdf; WFCA Roger Wilson Testimony.pdf; WFCA Scott Appel Testimony.pdf; Written Testimony from General Fox Regarding Alternatives to the Markplace Fairness Act.pdf; 72 TNI 49 .pdf; 140321_eBay_Ltr_to_House Judiciary.pdf; AinsworthR-MadzharovaB061413_000.pdf; AVALARA.PDF; FedTax Judiciary Committee Statement 031214.pdf; GeorgeChityatWrittenTestimony_FINAL.docx; House Judiciary Committee Written Statement 3-12-14.pdf; KevinHickeyWrittenTestimony_FINAL.docx; McKaneDavisWrittenTestimony_FINAL.docx; MFA Jim Walters Testimony.pdf; NCSL House Judiciary Committee Written Statement 3-12-14.pdf; NTU L14 03-12 House IST Hearing Comments - Final.docx; RER - internet sales tax hrg stmt 03 12 2014.pdf; RILA Written Comments for Record - House Judiciary Committee March 12 2014 Efairness Hearing.pdf; Testimony For House Judiciary Committee 3-17-14.docx; Testimony of Scott Humphrey WFCA.pdf; WFCA Charles Witt Testimony.pdf; WFCA Kelby Frederick Testimony.pdf

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FedTax Judiciary Committee Statement 031214.pdf GeorgeChityatWrittenTestimony_FINAL.docx
House Judiciary Committee Written Statement 3-12-14.pdf KevinHickeyWrittenTestimony_FINAL.docx
McKaneDavisWrittenTestimony_FINAL.docx
MFA Jim Walters Testimony.pdf
NCSL House Judiciary Committee Written Statement 3-12-14.pdf NTU L14 03-12 House IST Hearing Comments - Final.docx RER - internet sales tax hrg stmt 03 12 2014.pdf RILA Written Comments for Record - House Judiciary Committee March 12 2014 Efairness Hearing.pdf Testimony For House Judiciary Committee 3-17-14.docx Testimony of Scott Humphrey WFCA.pdf WFCA Charles Witt Testimony.pdf WFCA Kelby Frederick Testimony.pdf

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Testimony submitted to the

United States House of Representatives Committee on the Judiciary

Hearing on:

Exploring Alternative Solutions on the Internet Sales Tax Issue

March 4, 2014

Chairman Goodlatte, Ranking Member Conyers, and members of the committee: thank you for holding a hearing on Exploring Alternative Solutions on the Internet Sales Tax Issue.

I am Kevin Hickey, CEO of Online Stores, Inc., a New Stanton, Pennsylvania business that sells American Flags and other goods over the Internet. I appreciate that this hearing is taking place and that Chairman Goodlatte is taking a thoughtful approach on such a serious subject. I'd also like to thank the chairman for releasing principles that focus on minimizing regulatory burdens and ensuring that small online retailers are not subject to unfair proposals like the Marketplace Fairness Act. I'd like to share my personal experiences that lend support to the Chairman's efforts.

I've been through a sales tax audit in my home state of Pennsylvania and it was one of the most unpleasant experiences of my life. My audit experience is the foremost reason why I oppose the MFA and similar legislation.

People who have never been through a sales tax audit — including many members of Congress — simply don't understand what a nightmare it is. But I know the burdens and costs first hand.

My company has always collected Pennsylvania sales taxes and has never skirted the law. But when we were audited, the auditor was determined to find every possible way to extract money from us. She spent 160 hours sitting in our offices scouring over invoices in an effort to find errors and levy penalties on us.

She cited obscure, confusing, and often contradictory case law to try and prove we had skirted the law. We sell American flags and U.S. military flags online and through a catalog. Even though the Pennsylvania law clearly states that these items are tax exempt, the auditor insisted that historical U.S. flags and official U.S. military flags are not exempt. She also asserted that all shipping charges were taxable, even when orders included products that were tax exempt. But the case law was unclear on this issue – and still is! It didn't matter. She fined us for nonpayment and noncompliance.

When she was done, she handed us a bill for over $25,000 dollars for uncollected sales taxes, penalties, and interest. The entire $25,000 was due immediately and she told us that if we disagreed with her findings, we had to file an appeal with the state Department of Revenue. We did appeal the ruling and that appeals process was frustrating, time-consuming, and costly. We did finally win most of the issues we appealed on, and we were refunded $15,000. The true cost was the many hundreds of hours of management time my staff and I were forced to spend on this nonproductive and very frustrating distraction from running and growing our business.

Subsequent to the audit we found out that many of the things the auditor told us were either not true or were half-truths. We were not able to find experienced sales tax experts in our field to assist us in the audit.

If the MFA passes, this experience would be multiplied exponentially for thousands of small businesses like mine. We'll be vulnerable to auditors in states where we have no presence, no voting rights and no representation. To make matters worse, if we make mistakes, many remote

states can "pierce the corporate veil" and confiscate our personal possessions in order to satisfy their demands. In other words, we are personally responsible for the taxes whether or not we collect them from our customers. This is taxation without representation.

I do not believe my audit nightmare is an outlier. In fact, as I have talked to other online retailers I've realized that my experience is actually quite common, even the norm. Many accountants and tax attorneys have expressed reservations about the MFA for similar reasons. Thomas Mazurek, a CPA and state tax adviser with the accounting firm Tronconi, Segarra, and Associates recently expressed his concerns with the MFA, "I know how challenging and time consuming sales tax audits can be. I can't imagine how a small business will handle getting hit with multiple audits."

As small businesses, we are vulnerable targets for aggressive state auditors. In fact, many of us are already receiving letters and phone calls from other states' Departments of Revenue demanding that we disclose to them our sales data, employee data and even our confidential financial data. We have no presence in these states and yet they are already demanding access to our private data. This is a gross overreach of power and it illustrates what is coming if the MFA, or related legislation, passes. Even though no remote seller sales tax collection law has passed the US House, states have already budgeted for funds they believe the MFA, or related legislation, will raise. Make no mistake; the auditors are coming for us en masse unless our elected representatives protect us.

Scott Peterson, the former director of the South Dakota Department of Revenue's Business Tax Division, former executive director of the Streamlined Sales Tax Governing Board, and current employee of Sales Tax Software Provider Avalara, said that "few states audit more than 2 percent of their retailers in any given year." If you do the math, a ratio of even a 2% chance of audit in any state, multiplied by the 46 states that have sales tax, means that on average a remote seller could be audited almost every year. Based on my nightmarish audit experience - in a state where I even enjoy representation - you can see why I am so concerned about this issue.

Some believe that limiting the audits to "one per year" is an adequate solution. Remote businesses that only have physical presence in a single state should face the same risk of audit that any other business with physical presence in only one state faces - no more than a 2% chance of audit per year, on average.

Just because people from other states buy from us doesn't mean we should face increased risk of audit from remote states. People from one state travel to and buy from sellers in other states all the time, yet those sellers do not face any audit risk from the states the shoppers come from.

If Congress decides to put a destination-based tax collection requirement on remote sellers with audits from the destination states, it should require destination-based tax remittance for all brick and mortar sellers as well, subject to audits from the states where their buyers travel from. That

would be the only way to have - as proponents of the Marketplace Fairness Act say is their motive - a fair and level playing field.

I encourage Congress to protect small businesses and ensure that remote sellers will not face the prospect of any audit more than they do where they have physical presence - no more than a 2% chance, on average - nor should they be audited by any state where they do not have a physical presence nor access to elected representation.

BakerBros
area rugs & flooring • since 1945

Statement for the Record

Phil Koufidakis
President, Baker Brothers

to the

House Judiciary Committee

March 4, 2014

Chairman Goodlatte, Ranking Member Conyers and Distinguished Members of the Committee, my name is Phil Koufidakis. I thank you for this opportunity to provide this written testimony in support of the Marketplace Fairness Act ("MFA"). The Act is of great importance to me as an owner and operator of a brick and mortar retail business and is crucial to allow me to compete fairly with Internet sellers.

I am the owner and President of Baker Brothers. Baker Brothers is a full-service retail flooring company. The company has been family owned and operated since 1945. It has grown to seven retail locations and one trade location as listed below. Each retail store is approximately 10,000 square feet. Baker Brothers has 40 employees and hires a number of independent contractors to install flooring products for its customers.

I joined Baker Brothers in October 2003. Prior that, I was worked for several flooring manufacturers, including Philadelphia Carpets, Evans and Black, World Carpets and finally Stanton Carpets where I was VP of Sales. In September 2006 I bought Baker Brothers and have owned and operated the business ever since.

I submit this written testimony to explain the need for the Marketplace Fairness Act. My testimony is based on personal experience as a local brick and mortar retailer.

I. Unfair Competition by Internet Sellers

The Internet is a significant and often positive factor in the American economy. It can provide consumers with product information, expanded options and allow comparative shopping. My own company has embraced the Internet, developing websites for our stores, blogging on new products, advertising and using social networking. Accordingly, I do not wish to limit online selling. Rather, all I seek is to be allowed to compete fairly with my Internet competitors and that cannot happen when online businesses have a built in discount by not collecting the sales taxes that are due.

The problem is the inability of states like Arizona to enforce fully their sales tax laws to include Internet sales. This, in turn, gives the Internet seller an unfair advantage. This is not hypothetical for the flooring industry. Internet sellers actively advertise no sales tax.

Flooring is a high-ticket item costing thousands of dollars. As result, consumers generally want to see and touch the flooring before purchasing. With increasing frequency, I have seen an increase in Internet sales in the flooring industry. In some cases no matter what we do, my company cannot combat the sales tax issue. Even if the company meets the price at super low margins, the tax is often the difference between making and losing the sale. The company tries meet the price to avoid losing sales to the Internet, but ultimately all it does is lessen profit and sales commission, which ultimately puts less money in the local coffers.

Internet sales of flooring are increasing rapidly, especially with the introduction of easy to install floors. Today, a consumer can install a laminate floor that simply snaps together without the need for any glue or nails. Similarly, there are self-adhesive laminates, tiles and vinyl that can be installed by simply peeling off the back sheet and laying the floor tile in place. Shaw, the largest manufacturer of carpet, sells self-stick carpet tiles, making installation of wall-to-wall carpet easier. Mohawk, the other major manufacturer of carpet, offers a similar product. There are a host of other flooring products that a consumer can buy and install him or herself. The problem is not the availability of these products, but that Internet sellers are selling them with no sales tax, creating an unfair and unearned advantage over the local brick and mortar store.

The MFA provides a fair solution to this problem. The Act allows, but does not require, a state to have Internet sellers collect the sales tax just like local retailers do now. Accordingly, the Act put the decision where it belongs, at the local state level. Sales taxes are set at the state level to provide for local services and needs. These taxes pay for fire and police departments, libraries, parks and a host of other local projects and services. The loss of the tax on Internet sales can only lead to higher taxes to support these local needs.

II. House Judiciary Committee Basic Principles

I have addressed below the "Basic Principles on Internet Sales Tax" set forth by the Committee on September 18, 2013.

1. Tax Relief

Requiring Internet sellers to collect the existing sales tax does not create a new tax. The consumer owes the sales tax on all items he or she purchases whether at a local store or from a remote Internet seller. That is why it is not part of the price, but added to the final price of an item. The problem is there is no practical way to collect the tax unless the seller collects it at the time of the sale. The local retailer is obligated to collect the tax on all of its sales. All the MFA does is allow state to require that remote Internet sellers collect sales tax from its customers just like the local brick and mortar stores now do. Accordingly, the MFA does not create a new tax anymore than enforcing existing tax laws creates a new tax. Rather, it simply creates a practical means of collecting the taxes that are already due.

2. Tech Neutrality

As explained above, the current system puts brick and mortar at a distinct disadvantage to online and brick and click businesses. In effect, out-of-state Internet sellers have a "no sales tax discount." As established earlier, Internet sellers tout this "discount." Local brick and mortar stores must collect the tax, and that discount is often the difference between the local stores making a sale or losing a sale. The MFA, therefore, is essential for a fair free market to work in the flooring industry with all competitors operating on equal footing under the same rules.

3. No Regulation Without Representation

The seller does not pay the sales tax; it is paid by the consumer. These taxes are determined at the state and local level and are used to support local services and needs, such as fire and police departments, libraries and parks. The consumer, whether he or she buys locally or from a remote Internet seller, lives in the locations where the tax is due and benefits from the services for which these taxes pay. Requiring an Internet seller to collect the tax from these consumers is only fair. The Internet seller does not pay them. Rather, all that the MFA would do is authorize states to require Internet sellers to collect the tax so that the local consumer simply pays his or her fair share.

4. Simplicity

I do not see taxing Internet sales as creating a significant burden on the Internet seller. My company keeps track of, collects and remits the state and local sales tax in every location in the state where we do business. As a result, every month the company regularly applies, collects and remits to 10 to 12 sales tax rates depending on where the sale is made. With today's computer systems, the company can easily account for, collect, and remit the taxes collected for the different rates. The collection is not complicated with today's computer system. Arizona provides a website that enables business taxpayers to file and pay state taxes online.

An Internet seller will have no problems collecting and remitting sales taxes. The MFA would require a state to meet the standards for simplifying their sales tax rules, provide the Internet seller free software to implement the collection and remittance of the sales taxes that are already due on these sales, and allow Internet and mail order sellers to elect to register with the "one stop" system covering all participating states. The Act would not impose any burden on Internet sellers who are already savvy with computer systems. The online businesses already use computers get authorization for credit cards, to verify addresses for shipment, to track shipments and deliveries and to advertise their product online. A system to correctly calculate a sales tax based on the customer's location takes nothing more than inputting the customer's address. This could not be easier since the Internet seller already inputs the delivery location at the time of sale. Accordingly, it costs nothing, is easy to use and uses the address information the Internet seller already collected.

Compliance is sufficiently simple so no small business would have problems collecting and remitting the taxes. The software is free and uses the very information already collected by the Internet seller to determine the tax that must be collected. The Internet business can also elect to use a centralized one-stop multi-state registration system, further minimizing any burden.

The current MFA establishes an unnecessary small business exception for any entity with less than $1 million of Internet or mail order sales. This is far too large of an exemption. A $1 million is approximately the size of the gross sales of the average retail flooring dealer in the United States. There simply is no need for a small business exception.

5. States' Rights

State and local governments determine whether to have a sales tax and the amount of the tax. These taxes support the state and local services and government. The MFA does not require a state to implement a sales tax. To the contrary, the Act leaves it to the states and local jurisdictions to decide whether to implement a sales tax, the amount of the tax, if any, and even whether to participate the MFA and have remote sellers collect the tax. The MFA allows state and local officials who are accountable to local voters to make these decisions.

6. Privacy Rights

There should be no real privacy issues. As a local retailer, I already collect sales taxes without violating any privacy right of my consumer. Internet sellers' collecting sales taxes should create no new privacy concerns.

III. Conclusion

The MFA is needed to ensure fair competition, a cornerstone of the America capitalism, and to allow states to effectively collect the taxes that are already due on Internet sales. Without it, local retailers like me will continue to be at a disadvantage, local jobs will be lost, tax revenue already owed will not be collected and local communities will suffer. The MFA offers a fair solution without imposing unfair burdens on the Internet seller. To the contrary, the Act will allow a level playing field for all competitors, whether a put brick and mortar store, exclusively an online retailer or a brick and click business.

Attachment 1

Store Locations

Baker Bros
16950 N. 51st Avenue
Glendale, AZ 85306
Arizona 9th District: Rep. Trent Franks

Baker Bros
12483 West Bell Road
Surprise, AZ 85374
Arizona 9th District: Rep. Trent Franks

Baker Bros
3719 East Bell Road
Phoenix, AZ 85032
Arizona 6th District: Rep. David Schweikert

Baker Bros
835 E. Camelback Road
Phoenix, AZ 85014
Arizona 9th District: Rep. Kyrsten Sinema

Baker Bros
4909 West Chandler Blvd.
Chandler, AZ 85226
Arizona 9th District: Rep. Kyrsten Sinema

Baker Bros
1702 S. Val Vista
Mesa, AZ 85204
Arizona 5th District: Rep. Matt Salmon

Baker Bros
5090 North Hayden Road
Scottsdale, AZ 85250
Arizona 6th District: Rep. David Schweikert

Johnston
PAINT & DECORATING
SINCE 1925

3409 Buttonwood Dr., Columbia, MO. 65201
Phone (573) 443-8755 Fax (573) 875-8441

Statement for the Record

Melissa Murphy
Johnston Paint and Decorating

to the

House Judiciary Committee

March 4, 2014

Chairman Goodlatte, Ranking Member Conyers and Distinguished Members of the Committee, my name is Melissa Murphy. I thank you for this opportunity to provide this written testimony in support of the Marketplace Fairness Act ("MFA"). The Act is of great importance to me as an owner and operator of a brick and mortar retail business and is crucial to allow me to compete fairly with Internet sellers.

I am the owner of Johnston Paint and Decorating located in Columbia, Missouri. Johnston Paint and Decorating was started in 1925 as a family owned paint and wallpaper store. Still a locally owned family business, Johnston has grown to include selling tile, carpet, window treatments and custom draperies in addition to paint and wallpaper. Today Johnston's boasts a staff of 22 and contracts with local independent installers and remodelers who install and apply their products in commercial and residential settings.

I submit this written testimony to explain the need for the Marketplace Fairness Act. My testimony is based on personal experience as a local brick and mortar retailer.

I. Unfair Competition by Internet Sellers

It is not the Internet that I am opposed to, but the unfairness of allowing Internet sellers to compete for the same customers, buying the same products without requiring Internet companies to comply with the same rules that I must obey. I have myself embraced the Internet, developing websites for my stores, blogging on new products, adverting and using social networking. Accordingly, all I seek is to be allowed to compete fairly with my Internet competitors.

The problem is the inability of states like Missouri to enforce fully their sales tax laws to include Internet sales. This, in turn, gives the Internet seller an unfair advantage. This is not

hypothetical for the flooring industry. Internet sellers actively advertise no sales tax. For example, [PROVIDE SAMPLES OF INTERNET ADVERTISING OF NO SALES TAX][1]

Internet sales are a growing problem for retailers like Johnston Paint and Decorating. The complete lack of in-home service does not stop consumers from shopping online, in efforts simply to "save" a few bucks. With online retailers boasting "no sales tax," consumers are starting their remodel jobs with friendly brick and mortar retailers, and giving the final sale to the lowest online competitor. Currently wood flooring jobs are Johnston's most frequently lost sale to online competitors. Their average size wood floor sale is 750 square feet. With a median price of $6.00 per square foot that is a $4,500 sale, with a sales tax of $360 at the current Missouri sales tax rate of 8%. That price difference often results in a lost sale, and each one of these lost sales equates to a large loss of revenue for Johnston, the commissions for the salesperson and local taxes.

The problem is equally as detrimental for their wallpaper sales. Johnston Paint and Decorating's premier 22,000 square foot store has become a "showcase" for Internet sellers. Consumers go to the store, check out sample books only to use them to order wallpaper online. It has become so problematic that Johnston has had to limit consumer check out time to one day. With the 8% "sales tax discount" Johnston simply cannot compete with Internet pricing, and therefore wallpaper sales have suffered greatly.

Paint sales too have been a problem notwithstanding Johnston's supplier's efforts to improve the company's ability to compete with online sellers. Benjamin Moore, Johnston's flagship paint brand, has attempted a site-to-store concept where customers can order paint online and pick it up in their local store. Even though Johnston Paint and Decorating is Benjamin Moore's largest single store operation in a seven-state region, the store has filled only two orders in the past few months under this program. The store suffers lost sales; the employees suffer lost wages and commissions; and the state and local community suffer lost revenue needed to support local services and programs. Johnston Paint and Decorating can compete with any competitor if the playing field is fair. Unless Congress allows states to collect sales tax from Internet sellers, the viability of brick and mortar stores like Johnston Paint and Decorating will suffer, resulting in lost local jobs and income.

The MFA provides a reasonable solution to this problem. The Act would allow, but not require, a state to have Internet sellers collect the sales tax just like local retailer do now. Accordingly, the Act put the decision where it belongs, at the local state level. Sales taxes are set at the state level to provide for local services and needs. These taxes pay for fire and police departments, libraries, parks and a host of other local projects and services. The loss of the tax on Internet sales can only lead to higher taxes to support these local needs.

II. House Judiciary Committee Basic Principles

I have addressed below the "Basic Principles on Internet Sales Tax" set forth by the Committee on September 18, 2013.

1. Tax Relief

The MFA is not a new tax. The consumer owes the sales tax on all items he or she purchases whether at a local store or from a remote Internet seller. That is why it is not part of

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[1] *See* samples of no sales tax advertising attached hereto as Attachment 2.

the price, but added to the final price of an item. The problem is there is no practical way to collect the tax unless the seller collects it at the time of the sale. The local retailer is obligated to collect the tax on all of its sales. All the MFA does is allow the state to require remote Internet sellers to collect the sales tax from its customers just like the local brick and mortar stores now do. Accordingly, the MFA simply creates a practical means of collecting the taxes that are already due.

2. Tech Neutrality

As explained above, the current system does not put brick and mortar, exclusively online and brick and click businesses on equal footing. Brick and mortar stores are at a distinct disadvantage. In essence, out-of-state Internet sellers have a "no sales tax discount." Internet sellers tout this "discount" in competing for sales. Local brick and mortar stores must collect the tax, and that discount is often the difference between the local stores making or losing a sale. The MFA, therefore, is essential for a fair free market to work in the flooring industry to provide that all competitors operating under the same rules.

3. No Regulation Without Representation

The consumer, not the Internet seller, pays the sales tax. That consumer is part of the local community that elected the state and local officials who determined the amount and the use of the sales taxes collected. That consumer enjoys the local services, such as fire and police departments, libraries and parks, that the sales tax supports. All that the MFA would do is authorize states to require Internet sellers collected—not pay— the tax. The local consumer buying online would simply pay his or her fair share.

4. Simplicity

Taxing Internet sales will not impose a significant burden on the Internet seller. With today's computer systems, a company can easily account for, collect and remit the taxes collected. Internet sellers already use with computer systems extensively, using them to verify addresses for shipment, get authorization for credit cards, and to advertise their product online. A system to correctly calculate a sales tax based on the customers location takes nothing more then inputting the customer's address. This could not be easier since the Internet seller already inputs the delivery location at the time of sale.

In addition, the MFA would actually make the system easier and more streamlined. To use the authorization to collect the sales tax, a state must simplifying their sales tax rules, provide the Internet seller free software to implement the collection and remittance of the sales taxes that are already due on these sales, and allow Internet and mail order sellers to elect to register with the "one stop" system covering all participating states.

Accordingly, it costs nothing, is easy to use and uses the information the Internet seller already collected, such as the consumer's address for delivery. The MFA would not impose any significant burden on small business. As a result, the current a small business exception in the MFA for any entity with less than $1 million of Internet sales is not needed. This is far too large of an exemption. If $1 million is the definition of "small business" than many, if not a majority of, retail flooring stores would be small businesses. Yet these very brick and mortar stores are constantly facing the unfair competition from Internet sellers who do not, and in fact tout that they do not collect sales taxes.

5. States' Rights

The implementation and amount of any sales tax are purely a local determination. The MFA does not change that. State and local officials, who must answer to local constituents, will still determine whether there will be a sales tax, the amount of the tax and even whether to participate the MFA and have remote sellers collect the tax.

6. Privacy Rights

I am unaware of any privacy issues that would be caused by the MFA. As a local retailer, I already collect sales taxes without violating any privacy right of my consumer. Internet sellers' collecting sales taxes should create no new privacy concerns.

III. Conclusion

The MFA is needed to ensure fair competition, a cornerstone of the America capitalism, and to allow states to effectively collect the taxes that are already due on Internet sales. Without it, local retailers like me will continue to suffer, local jobs will be lost, tax revenue already owed will not be collected and local communities will suffer. The MFA offers a fair solution without imposing unfair burdens on the Internet. To the contrary, the Act will allow a level playing field for all competitors, whether a put brick and mortar store, exclusively an online retailer or a brick and click businesses.

Draft

STATEMENT OF RORY RAWLINGS
Founder and Chief Tax Automation Officer
Avalara

Before the U.S. House Committee on the Judiciary
Washington, DC
DATE, 2014

Chairman Goodlatte, Ranking Member Conyers, and Members of the Committee: Thank you for providing the opportunity to testify today. My name is Rory Rawlings and I am a founder and the chief tax automation officer for Avalara – an automated sales tax compliance service provider based in Bainbridge Island, Washington. I am here to share Avalara's views on specific provisions that we believe should be included in any House remote sales tax bill and are consistent with Chairman Goodlatte's "Basic Principles on Remote Sales Tax" ("Committee's Principles") issued on September 18, 2013. If a remote sales tax bill were to become law, there would be no technological, implementation, or compatibility issues that would keep online businesses or remote sellers from complying with their obligation to collect and remit sales and/or use taxes. In fact, we currently help thousands of businesses across the country comply with sales and other transactional tax obligations.

For more than 10 years, Avalara has been addressing a need among small and mid-sized business for an affordable way to manage the transactional tax compliance process. We pioneered a web-based platform that provides automated end-to-end tax compliance services, including instantaneous rate and taxability rule determination, returns preparation and remittance, and exempt certificate management. Avalara now employs more than 550 professionals, with offices in Bainbridge Island and Seattle, Washington; San Diego, Rocklin, and Irvine, California; Falls Church, Virginia; Raleigh, North Carolina; Harrisburg, Pennsylvania; Pune, India; and the United Kingdom.

Avalara is not the only provider of technology solutions that assist businesses and remote sellers in meeting their sales tax related compliance obligations. We have numerous well-established competitors in a broad and growing market. For businesses operating in multiple jurisdictions, sales tax compliance can be exceedingly complex, and multiple technology solutions have been developed to address this complexity.

Avalara's web-driven solution begins by calculating an online purchaser's tax rates with "roof top" accuracy. This means that by using precise address validation and geo-location technology, we can pinpoint a transaction within all jurisdictions that apply to a sale. Our tax engine then identifies product taxability, determines relevant tax rates, verifies the exemption status of the purchaser, and returns an accurate tax calculation in real time – usually less than one second. The speed of this calculation is important for all businesses, regardless of their sales process, but it is obviously critical in the case of ecommerce shopping carts.

All of this transaction data is securely stored to facilitate the returns preparation and remittance process, which can be just as complex and difficult as accurate calculation, if not more so. Our technology allows customers to extract reports and manage their returns process manually, but we find that most prefer to utilize our automated service as a simple extension of the value we provide.

Avalara's technology and statutory sales tax content encompass tens of thousands of taxability rules, a library of more than 10 million taxability-researched products organized by uniform product codes (UPC), and millions of product-specific and business entity tax exemptions. We also maintain hundreds of state tax return and exemption certificate forms for instant use in the compliance process. Our engine automatically applies this content to deliver tax decisions covering more than 152 million U.S. mailing addresses located within more than 11,000 taxing jurisdictions. This provides a fast, easy, accurate, and affordable way for online businesses and other remote sellers to manage transactional tax obligations.

I. Avalara's Technology Integrates Seamlessly with Online Businesses' and Remote Sellers' Pre-existing Business Systems

We are aware that online businesses and remote sellers have expressed concerns regarding how to implement possible remote sales tax requirements and integrate 46 different state software schemes with their pre-existing business systems. There also is an understandable apprehension about satisfying the requirements of over 11,000 different tax jurisdictions.

At Avalara, we address these concerns by providing hundreds of pre-built connectors into the financial, billing, ecommerce, or point of sale systems our customers already use to run their businesses. Additionally, we provide open access to our service for the purpose of developing custom integrations. Services like ours obviate any need for remote sellers to integrate with separate state software programs and as discussed earlier, our technology automatically returns accurate tax decisions for transactions across all US taxing jurisdictions.

II. Avalara's Legislative Concerns

There are two specific issues of concern that Avalara not only strongly believes should be included in any House remote sales tax bill language, but also are consistent with this Committee's Principles.

a. Remote Sellers Should Retain the Right to Choose a Software Provider, and Not Be Coerced to Use State Sponsored Software

Avalara's first issue of concern is that House remote sales tax bill language, like the Senate's Marketplace Fairness Act (MFA), should ensure that online businesses and remote sellers have a fundamental right of choice in selecting and using the software provider that works best for their pre-existing business systems. Simply put, states should not be permitted to force remote sellers to use specific state-sponsored or operated tax software any more than they should be able to require individual taxpayers to use a specific tax preparer's product for their individual income tax returns. I certainly wouldn't want the states to force me to be reliant on a state-

sponsored tax preparation software program rather than using H&R Block, Intuit, or any other provider. Permitting remote sellers to utilize internet sales tax software and services of their own choosing will encourage competition and innovation, and drive down prices for such services.

The right of choice would also ensure that online businesses and remote sellers can select a tax software/service vendor that is compliant with state standards. As previously mentioned, remote sellers will need a service that gives them an effective way to deal with 46 states and innumerable local jurisdictions with different sales taxes. Avalara believes that only private sector companies can provide such a service, and remote sellers should not be required to use each state's software, which may not integrate with other states' software.

The remote sellers' right of choice in selecting a software provider is consistent with two of the Committee's Principles. First, the *Simplicity Principle*, which highlights that governments should not stifle businesses by shifting onerous compliance requirements onto them and touts simple and inexpensive compliance with laws. Second, the *Tech Neutrality Principle*, which asserts that the sales tax compliance burden for online internet sellers should be equivalent to similarly situated offline businesses. U.S. Senator Mike Enzi also recognized that remote sellers' right of choice is absolutely vital. He offered a perfecting amendment to the MFA, S. 743, which was adopted by a vote of 70-24, prior to the bill's final passage on May 6, 2013.

Using S. 743 as an example, Avalara would recommend the following insertion to Section 3 (page 8, lines 5-8) of the legislation:

> "(c) NO EFFECT ON SELLER CHOICE. – *Nothing in this Act shall be construed to deny the ability of a remote seller to deploy and utilize a certified software provider of the seller's choice.*"

b. Improper Shifting of Liability for Unpaid Tax Obligations to Certified Software Providers Like Avalara

The second issue Avalara believes must be addressed in any House remote sales tax bill language is liability for unpaid tax obligations. Avalara believes the onus of a remote seller's unpaid sales or use taxes should remain with the seller and not contractually transfer to the software provider. Today, some states enter into agreements with software providers that require, or more accurately, force the software providers to accept legal liability for remote sellers' unpaid tax obligations, even if the software provider has committed no error. For example, when states audit remote sellers, they often challenge transactions (sometimes thousands of transactions), which the seller has claimed are exempt from sales or use taxes. Under various state laws, the software provider – not the remote seller – must prove within a short period of time (typically 60 to 120 days) that the transactions were exempt, even if the transactions occurred years before the audit or the remote seller has subsequently gone out of business. If the software provider cannot prove that such transactions were exempt, it is liable to the state for unpaid sales and/or use taxes.

Avalara believes that shifting the liability for unpaid tax obligations to service providers such as Avalara creates a burdensome and inequitable result that must be eliminated in any piece

of remote sales tax legislation. Correcting this problem is also consistent with the Committee's *Simplicity Principle*, underscoring that businesses should not be stifled by onerous compliance requirements. In order to be consistent with the Committee's Principles, and to ensure fairness and equity, we recommend that any remote sales tax bill language contain certain provisions relating to critical liability issues. Using S. 743 as an example, Avalara would recommend the following changes:

(1) Page 5, Line 25, after the period, insert the following:

"The certified software provider's liability shall be no more than the compensation due and payable to the certified software provider under its agreement with the remote seller."

(2) Page 9, after Line 7, insert the following new subsection:

"(h) Seller Liability for Nonpayment of Taxes. – Notwithstanding any other provisions of federal or state law, a remote seller shall be liable for the nonpayment of state or local sales or use taxes, except where such nonpayment is the result of an error or omission made by a certified software provider."

In conclusion, Avalara believes it is vital that any House remote sales tax bill language should (1) protect remote sellers' right of choice in selecting a software provider and (2) prevent the shifting of liability for unpaid tax obligations. Lawmakers cannot, and should not, expect online businesses and remote sellers to possess the capability to adhere to any internet sales tax law without the availability of proper technology solutions. We believe it should be a Congressional priority to safeguard competition and equal footing in the marketplace by not favoring or requiring one software provider product over another or shifting liability for unpaid tax obligations to software providers. Both of these issues and concerns fall squarely within the Committee's Principles and we feel their inclusion in bill language would strengthen the remote sales tax framework moving forward.

I would like to once again emphasize that if a remote sales tax bill were to become law, there would be no technological, implementation, or compatibility issues that would prevent online businesses or remote sellers from selecting from a range of commercially available automation products and services and very quickly implementing them.

Thank you again for receiving my testimony and I look forward to answering your questions.

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Written Testimony by

The Retail Industry Leaders Association (RILA)

Before the House Judiciary Committee

Hearing on "Exploring Alternative Solutions on the Internet Sales Tax Issue"

March 12, 2014

2141 Rayburn House Office Building

Washington, DC 20515

On behalf of the Retail Industry Leaders Association (RILA), thank you for holding this hearing entitled "Exploring Alternative Solutions on the Internet Sales Tax Issue" and for providing your colleagues and the public with the opportunity to discuss options for addressing the inequity that Main Street merchants experience due to the disparate treatment of how sales taxes are collected on online and via other remote purchases. Simply holding this hearing is an indication that there is widespread agreement that this issue needs to be solved before another holiday shopping season passes. While RILA supports the Senate-passed Marketplace Fairness Act (S. 743) and its House companion (H.R. 684), we acknowledge that there may be different ways to address this issue, which is why RILA has engaged with the Judiciary Committee to provide thoughtful solutions and options for the Committee to consider. We hope that following the hearing the Committee quickly proceeds to drafting legislation with the same sense of urgency that our retailers have for creating a level playing field with respect to sales tax collection on online purchases.

By way of background, RILA is the trade association of the world's largest and most innovative retail companies. RILA promotes consumer choice and economic freedom through public policy and industry operational excellence. Its members include more than 200 retailers, product manufacturers, and service suppliers, which together account for more than $1.5 trillion in annual sales, millions of American jobs and more than 100,000 stores, manufacturing facilities and distribution centers domestically and abroad.

This opportunity before Congress has been a long time coming. The current system of sales tax collection is complicated and arcane. It does not resonate in a 21st century global economy that no longer recognizes old borders. Now is the time for Congress to instill simplicity upon the current state sales tax collection regime to allow all sellers to collect and remit on behalf of their consumers and to shift the burden from individual consumers who are currently obligated to track and remit use taxes themselves.

A sale is a sale is a sale. Whether it takes place online or at a local business, the same tax rules should apply online as they do on Main Street. Common sense would dictate that if a product is

purchased online, the retailer should collect and remit sales tax to the customer's state, just as is the case when a customer goes to the store in person.

Due to a decades-old loophole that pre-dates the Internet (the result of the 1992 *Quill* Supreme Court decision), online-only companies can achieve as much as a 10 percent price advantage over brick and mortar retailers by refusing to collect and remit the state and local sales tax owed on purchases made online. This special treatment has the effect of the government picking winners and losers in the marketplace, and local businesses simply cannot compete over the long-term with online giants that exploit this government-sponsored loophole. In addition, this government-sponsored loophole has the effect of distorting purchasing habits in the marketplace; if all merchants are required to collect sales taxes on all online purchase, then competitive forces such as consumer choice, service and price would be dictating spending decisions rather than tax policy distorting consumers preferences based on whether a company's website has to collect a sales tax or not.

For RILA, as well as millions of Main Street brick and mortar businesses, the top priority for the industry is to level the playing field on the collection of sales taxes between brick and mortar retailers and remote sellers and to create a less complex system of sales tax collection. Of the 45 states that collect sales taxes, 43 of them have taken some sort of legislative action to partially level the playing field. States such as California, Texas, Illinois, Pennsylvania, Virginia, Georgia, Tennessee, Indiana, and Nevada, to name a few, have already passed state legislation or taken administrative action to expand their state's definition of physical nexus for sales tax collection purposes thereby creating a patchwork quilt of complex, and at times, differing definitions of physical presence. In the absence of federal action, states will continue to further expand their definitions to capture more online retailers which further complicate an already antiquated system.

States such as Wisconsin, Ohio, Utah, and others have taken bold action to pass legislation that stipulates that upon enactment of the Marketplace Fairness Act – or an equivalent bill granting remote collection authority – budget neutral tax cuts take effect for the state. In Wisconsin, Governor Scott Walker signed into law a bill that will automatically trigger a state income tax

cut for individuals, families and small businesses upon enactment of e-fairness legislation. In Ohio, state legislators worked with Governor John Kasich to include a provision in their 2014 budget bill that directs revenue gained from passage of e-fairness legislation to Ohio's income tax reduction fund. In Utah, legislators and Governor Gary Herbert have put in place a mechanism to direct any additional revenue received from e-fairness into a restricted fund which will be allocated to lower the overall sales tax rate.

The macroeconomic effect of passing e-fairness legislation has economy-wide benefits according to a seminal study published by conservative economists Art Laffer and Donna Arduin in July 2013. The study, entitled "Pro-Growth Tax Reform and E-Fairness," found that if Congress enacted e-fairness legislation and states choose to wisely use the revenue to broaden the base and lower rates – essentially as Wisconsin, Utah and Ohio have contemplated – there would be an economy-wide benefit to the U.S. of $563.2 billion in increased GDP and the creation of approximately 1.5 million jobs over the next decade. Laffer and Adruin write that "Addressing the e-fairness problem from a pro-growth perspective creates several benefits for the economy," including that "all retailers would be treated equally under state law" and that states would be given "the opportunity to make their tax systems more efficient and to increase competition amongst all retailers."

Because of the constitutional issues in the *Quill* decision associated with the Commerce Clause, states cannot completely level the playing field on their own: federal legislation is required. In fact, in its decision in *Quill,* the Supreme Court invited Congress to exercise its authority to solve this problem and let the states enforce their laws to level the playing field. Writing for the majority, Justice John Paul Stevens wrote, "This aspect of our decision is made easier by the fact that the underlying issue is not only one that Congress may be better qualified to resolve, but also one that Congress has the ultimate power to resolve. No matter how we evaluate the burdens that use taxes impose on interstate commerce, Congress remains free to disagree with our conclusions." Moreover, the U.S. Supreme Court recently sidestepped the issue when it declined on December 2, 2013, to grant certiorari on two cases brought by online-only retailers Amazon.com and Overstock.com challenging New York's affiliate nexus laws. In April 2008, New York State expanded its definition of physical nexus by enacting a law requiring certain

remote sellers to collect sales taxes for sales made to residents in the state if the retailer had advertising affiliates helping to facilitate the sale of goods. Amazon.com and Overstock.com brought separate cases challenging the statute and New York ultimately prevailed after appeals were exhausted by lower courts. The December 2013 decision by the Supreme Court to avoid the issue is a clear message to Congress that the courts cannot and will not solve this issue and that Congress must do the inevitable and take action.

Unless the current system is corrected, local retailers – big and small – will increasingly be forced to close their doors, taking with them the millions of retail jobs they provide as these businesses are punished for following the law while their online competitors are exempted. From local booksellers and jewelers to national chains, the tilted playing field has already cost tens of thousands of local jobs and more are threatened the longer this disparity continues. These businesses provide crucially needed jobs, pay local property taxes and make critical civic investments in our communities. Punishing local businesses in favor of out of state business runs counter to the government's efforts towards building local communities that are vibrant and healthy. As brick and mortar stores look ahead to whether to renew their leases in shopping centers and communities across the country they will be looking to whether Congress acts to level the playing field.

Further, this is a matter of states' rights. A state should be able to enforce their laws regardless of whether a product or service is purchased from an in-state or out-of-state vendor. Congress should allow states to enforce their own laws, taking the federal government out of the business of picking winners and losers. States can also choose to lower other taxes with e-fairness collections. At a time when nearly every state is facing significant budget shortfalls, states are considering increasing sales and property taxes to close these gaps, which have the effect of further widening the disparity between brick and mortar stores and remote vendors. According to the National Conference of State Legislatures, over $23 billion dollars in sales taxes will go uncollected this year alone even though consumers still owe the corresponding use tax. As the Internet continues growing as a retail platform, this collection gap will only grow larger.

It should be noted that closing this loophole cannot be construed as a new tax. Just because

some online-sellers do not currently collect the tax does not mean the state's sales or equivalent use tax is not still due. In fact, today online-only establishments are leaving individuals who purchase items on their websites exposed to audits and penalties since these consumers are still legally responsible for tracking their purchases and paying the tax owed directly to the state.

But to be clear, opposition to e-fairness legislation isn't coming from truly small online sellers because they are exempted from the Marketplace Fairness Act and can be reasonably expected to also be exempted from other similar bills. According to a Small Business Administration (SBA) report released in November 2013 entitled "An Analysis of Internet Sales Taxation and the Small Seller Exemption," the SBA found that "With a [small seller exception] of $1 million, only a very small number of companies would actually be required to collect and remit sales taxes..." In fact, the authors of the report estimated that at a $1 million exemption level, only 1,817 companies would be covered by various legislative proposals, representing 0.04 percent of all retailers. In other words, 99.96% of all sellers would be exempted. For those sellers that sell over and above any exemption level determined by Congress, they could choose to use any of the readily available sales tax collection software products available for use today, including one available for use by eBay sellers today by a company called Avalara. Avalara's AvaTax software costs as little as $15 per month and is fully integrated with eBay's online shopping cart system.

This is why important business simplifications were included in the Marketplace Fairness Act and should likewise be included in any similar legislation. For example, previous bills have: provided for free software, provided by the states, for remote sellers; uniform rates and tax bases within a state; consolidation of where, within a state, sales taxes should be filed and remitted; and other important simplifications. In addition, previous e-fairness bills have had robust small seller exemptions, such as the $1 million exemption in S. 743, which ensures that small mom and pop and startup businesses are exempted until they have reached a mature level. The important business simplifications, when combined with the small seller exemption, allow Congress to address this issue without burdening interstate commerce. RILA would support additional simplification measures and business protections as the Committee moves forward on this issue.

In closing, RILA appreciates the opportunity to submit this written testimony for the record. Congress should immediately pass e-fairness legislation in order to ensure a level playing field that protects jobs on Main Street, reduces budgetary pressure on states to further increase sales and property taxes, empowers states to cut taxes from closing the online sales tax loophole, and shifts the burden of collecting and remitting the use tax from individual consumers to online sellers. A comprehensive federal approach should allow the state, individually or through an interstate compact, to simplify their sales tax laws. This solution would simply provide self-help for the states, and it would do so without adding a penny to the federal deficit. Bipartisan bills such as the Senate-passed S. 743, H.R. 684 in the House, and any future bills originating from this Committee, can solve this problem and put home town businesses on a level playing field with online-only sellers. And when Congress enacts e-fairness legislation, it can take credit for creating 1.5 million jobs and adding $563.2 billion in GDP over the next decade as economists Laffer and Arduin have estimated. There is no good reason why Congress should wait until another holiday shopping season has passed before moving forward with a common-sense solution.

National Taxpayers Union

March 12, 2014

The Honorable Bob Goodlatte, Chairman
The Honorable John Conyers, Jr., Ranking Member
Committee on the Judiciary
U.S. House of Representatives
2138 Rayburn House Office Building
Washington, DC 20515

Dear Chairman Goodlatte, Ranking Member Conyers, and Members of the Committee:

On behalf of National Taxpayers Union's (NTU's) 362,000 members, I write to offer comments for the record in regard to the Committee's hearing today, entitled "Exploring Alternative Solutions on the Internet Sales Tax Issue." We applaud the thoughtful approach the Committee has taken toward this matter, which has extremely serious implications for taxpayers.

As you know, National Taxpayers Union's members have long been concerned about the extraterritorial tax collection powers that could have arisen from the Streamlined Sales and Use Tax Agreement (SSUTA) and its predecessor, the Streamlined Sales Tax Project. More recently, we have expressed grave doubts over the constitutionality, administrability, and equitability of the Marketplace Fairness Act (MFA).

After more than a decade of attempts to conclude a pact among a sufficient number of member-states, it is time to acknowledge that SSUTA is a failure. Not only has there been underwhelming progress in simplifying states' often byzantine sales and use tax systems, the cartel envisioned under SSUTA would arrogate dangerous powers unto itself. In 2008 Steve DelBianco of the NetChoice Coalition perceptively noted that what started with an "original simplification vision of one-rate-per-state" is mutating into a "dual-sourcing scheme to accommodate both origin and destination based taxes at the same time." Little has changed since then to reassure policymakers of SSUTA's approach.

Nor would it appear that the Marketplace Fairness Act, which amounts to a federalized attempt at imposing a similarly disturbing regime, is any more advisable a route to addressing the question of remote sales. This legislation (S.743), which passed the Senate in May of 2013, is in NTU's opinion the single greatest threat to taxpayers currently under serious contemplation in the 113th Congress. Our reasons for opposing MFA are legion and could occupy page after page of analysis. However, the summary of our position, expressed in Vote Alerts, fact sheets, and other materials, bears repeating here:

- The bill would hinder tax competition among the states, and may even encourage governments to "round up" their levies. NTU believes that the competitive dynamic among states and localities has exerted a more positive influence on tax rates, bases, and administrative procedures than any other force, save Constitutional tax and expenditure limitations (TELs). Indeed, one could argue that even TELS would be weaker and less prevalent, were it not for the salutary pressure on states to distinguish their own pro-taxpayer fiscal policies from those of their neighbors.

- The Supreme Court's *Quill* ruling has prevented state tax collectors from aggressively reaching across their borders, but MFA would overturn this important protection against abuse of power. The bill's attempt to carve out a sales-tax only exception to this ruling likely won't survive long, and the way would be paved for state administrators to gain authority over other taxes. The physical presence safeguard helps to shield taxpayers from many types of aggressive policies that could affect income, property, and other taxes.
- S. 743 gives wide latitude to define taxable "nexus," including its controversial extension to online advertising affiliates. Even states not participating in MFA's framework would have new powers.
- MFA would heap heavy burdens upon small businesses, which would face the task of collecting and remitting to nearly 10,000 taxing jurisdictions. MFA's supporters have tried to mitigate these burdens with a "small seller" exception, which is paltry by comparison to other government definitions of what constitutes a small business. A 2006 PricewaterhouseCoopers study demonstrated that small businesses with sales between $1 million and $10 million still face enormous costs that would threaten profitability, causing significant harm to interstate commerce and the economy during an especially fragile time.
- MFA fails to acknowledge that so many of the "Main Street" businesses the proposal aims to protect are actually thriving *because of*, not in spite of, the Internet. E-commerce allows "mom and pop" firms to market their goods and services to the entire world, not just to their immediate neighborhoods. It also gives these entities a much wider range of options to purchase supplies and other inputs, maximizing their cost-efficiency and productivity. In 2012, research by The Boston Consulting Group found that "small and medium-sized companies that embrace the Internet in their business operations grew by 10 percent annually in the last three years, adding jobs as they did so."

Owing to these misgivings, we were quite pleased that Chairman Goodlatte decided that the House should take greater responsibility for deliberating MFA than the Senate did. The serious manner in which the Committee has undertaken this task is reflected in the seven principles for Internet taxation which Chairman Goodlatte and Regulatory Reform, Commercial and Antitrust Law Subcommittee Chairman Bachus offered last September. Their guidelines aim to keep taxes low, level the playing field for all businesses, preserve interstate tax competition, prevent out-of-state tax collectors from unaccountably auditing and harassing businesses and individuals, simplify the collection and remittance processes to minimize or eliminate compliance costs, protect consumer privacy, and maintain an appropriate balance of power between states and the federal government.

Based on these precepts, the many demonstrable defects of MFA should disqualify it from further consideration. The American people would wholeheartedly agree. In September of 2013, NTU and the R Street Institute released a poll of 1,000 likely voters conducted by the respected Mercury firm. The results confirmed not merely a reflexive dislike of taxes, but instead revealed that Americans have a sophisticated understanding of (and trepidation toward) the administrative implications of an MFA-style structure:

- By a 57 percent to 35 percent proportion, respondents opposed the imposition of a remote sales-tax collection requirement.
- Self-identified Republicans and conservatives disliked MFA by 2 to 1 margins. Independents opposed MFA by a 56 percent to 37 percent margin, Democrats by a 48-43 percent margin, and split ticket voters by a 58-36 percent margin.
- When respondents were informed "the proposed legislation would allow tax enforcement agents from one state to collect taxes from online retailers based in a different state," and that it would entail new tax collection obligations for businesses, the margins against it swung to 70 percent and 69 percent, respectively.
- When confronted with the best arguments in favor of the legislation and against it – e.g., an MFA regime would be "fairer" to brick-and-mortar retailers – more than 60 percent of respondents supported the anti-MFA arguments.

Based on all of these cautionary arguments, what type of policy toward taxation of remote sales could satisfy the seven principles that Chairman Goodlatte and Chairman Bachus articulated? Some would argue that despite its flaws, the existing structure, with sufficient modifications and commitments to helping citizens meet use tax obligations, could still answer to the purpose. Evidence from states that have proactively engaged consumers is somewhat encouraging. For example, several years ago California's Board of Equalization estimated that a letter campaign reminding taxpayers they may owe use taxes for Internet purchases would help revenue from these activities to grow to $183 million in 2011, $367 million in 2012, and $600 million annually by 2013. Alabama has tested a similar letter campaign with success, including instances of taxpayers voluntarily sending the state checks for several thousand dollars.

Nonetheless, we understand that many Members of Congress do feel compelled to fashion a federally-directed response to state taxation of remote sales. For this reason, we recommend that lawmakers consider legislation defining the ability of states to proceed with such taxation only within the bounds of what is known as "origin sourcing." Simply put, this method would confer an obligation upon a business, whether selling to consumers locally or remotely, to collect and remit sales only to the jurisdiction in which that firm is based.

Members of this panel will hear and read a lengthier treatment of this concept today from R Street Institute's Andrew Moylan, who until 2012 served with NTU as its Vice President of Government Affairs. From our perspective, however, we continue to agree with the advantages of such a system, which would also comport with the seven principles outlined by Chairman Goodlatte and Chairman Bachus. Among them:

1) True "Fairness." While differently defined among the details of state laws, by and large origin sourcing is already the governing model for most brick-and-mortar retailers. Even though many areas technically practice "destination sourcing" for these stores, in effect the "destination" is the consumer at the cash register. Applying this philosophy to remote sales would avoid the need for a complex web of transaction-monitoring among almost 10,000 taxing entities and treat "e-tailers" the same as traditional stores. On the other hand, the scheme proposed under MFA would unfairly force online sellers to quiz their customers about their tax domicile and send back a properly-calculated amount to each buyer's home state.

2) Administrability. Some proponents of MFA claim that the existence of "free" (likely taxpayer-funded) software would sweep away any compliance problems that a destination-based scheme would impose upon remote sellers. This would seem laughable to most Americans who have experience with the federal income tax system. After all, according to NTU's most recent "Taxing Trend" study, 9 out of every 10 taxpayers rely on preparers or software to get through the tax-filing process. Yet, the business and personal tax system still imposes a deadweight loss on the economy conservatively estimated to exceed $240 billion.

As a recent NTU podcast with online retail entrepreneur Josh Olivo recounted, software is only a small part of the Internet sales tax compliance picture: it must somehow be seamlessly integrated into each business's existing systems. And despite MFA's promise of simplification, states' varying sales tax definitions and regulations could still mean many compliance headaches.

Moreover, the very real prospect of states' tax authorities reaching across their borders to audit and otherwise intimidate remote sellers elsewhere is daunting to small businesses. Olivo described how dealing with just one state's sales tax enforcement arm can slow his daily business development to a crawl. Giving 44 states' other auditors a chance to investigate him as well could deal a crippling blow to the future of his firm. Bruce Phillips, a CPA and managing member of a company specializing in small business compliance issues, recently told Fox News that "Sales tax audits can be just as bad or worse than IRS audits – and imagine you could have 10 to 20 auditors going through all of your sales!" It is therefore no wonder a coalition of small and medium-

sized e-tailers affirmed this and other fears about compliance overhead with hard numbers in an open letter to Congress, warning lawmakers that MFA could cost the signatories some 220,000 jobs. They characterized the MFA as "a weapon for Big Retail to crush Small Business."

3) Fiscal Federalism. Because origin sourcing would simply apply each state's existing tax rate and collection system for traditional retailers to every seller (even remote ones) located within their borders, the current balance of fiscal policies that every non-federal government has undertaken would remain in effect. All states would still have the prerogative to experiment with whatever taxation options are deemed most efficient and effective for its particular circumstances, provided it does not do so in a way that impedes commerce with its neighbors or across the nation generally. It is also entirely within the constitutional prerogative that the federal government can and should exercise: ensuring that the "laboratory of the states" functions to the benefit of all citizens and businesses while restraining predatory practices that would amount to tax enforcement without representation. In any case, as Professor Walter Hellerstein noted in 2012 testimony before the Senate Finance Committee, Congress already can and does limit the taxing activities of states in a number of ways. Among these are forbidding higher state taxes on air and motor carriers than on other businesses, restricting the application of stock transfer taxes, and prohibiting the levy of state taxes on the retirement income of non-residents.

An important step Congress could take to clarify the balance of state and federal tax policy would be to pass the Business Activity Tax Simplification Act (H.R. 2992), which was the subject of hearings late last month before the Subcommittee on Regulatory Reform, Commercial and Antitrust Law. The legislation would better define the concept of physical presence and set firmer proscriptions on state taxation of interstate commerce (including intangible property and services).

One aspect of the debate over alternative solutions to the Internet sales tax issue which should *not* excessively occupy Members of this panel is the question of state revenues. As other witnesses will explain to you in-depth today, the prospect of tens of billions of dollars in "lost" collections to the states has depended upon a highly-flawed methodology developed by the University of Tennessee that overstates the likely amount of revenue at stake. Furthermore, the "doomsday scenario" of massive business flight to zero-sales-tax jurisdictions concocted by opponents of origin sourcing is, in our opinion, unconvincing. For one, some of the states without broad-based sales taxes today offer unattractive rates of income and other taxes that might deter some businesses from making such a move.

Still, it is quite possible that some remote-selling firms will relocate to more hospitable retail tax climates. Yet, this is the essence of tax competition. The response to it is not to "lock down" businesses in their current locations, but rather to develop reasonable tax policies that will persuade them to remain where they are. This is a central task that should occupy not only states, but Washington, DC as well. Indeed it already has done so, as evidenced by the recent blueprint for a more internationally competitive federal tax system that your colleagues on the Ways & Means Committee unveiled in February.

Nor should Members of this panel who would describe themselves as "fiscal conservatives" be lured into believing claims that MFA-style legislation could finance some massive wave of pro-growth tax reforms among states. In an analysis of this argument – made in a study by economists Art Laffer and Donna Arduin late last year – NTU determined that the likelihood of states plowing every penny of a supposed $47 billion tax collection windfall into corresponding reductions in other taxes (thereby adding over $563 billion to economic output) was problematic at best. Indeed, Laffer and Arduin themselves provided contradictory evidence to suggest that at least eight states, among them California, New York, and Massachusetts, would likely use their new-found gains to grow government. This immediately shrank the supposed economic benefit by nearly one-third. They could only name Governors in two states – Wisconsin and Ohio – who at that time had formally

committed to using MFA for tax reform. As Chairman Goodlatte is well aware, another state's Governor – Virginia's – endorsed a tax-hike package in 2013 that countenanced passage of MFA to underwrite infrastructure programs instead.

It has been suggested that one potential model to deal with remote sales could be the current fuel-tax compact that governs interstate operations of motor carriers. In our opinion, this plan would at least offer one advantage over MFA: it would require governments themselves to directly shoulder the collection and remittance obligations that would otherwise be foisted upon remote sellers. We submit that this would give public officials a more direct appreciation of the opportunity costs that destination sourcing would have on each state's economy … and, perhaps, an incentive to abandon the entire exercise as unworkable. We would caution, however, that this approach should not be made mandatory for states that currently do not have sales taxes.

Others have suggested creating a reporting system for remote sales that governments, in turn, could utilize to collect taxes due. To us this would not entirely ameliorate the heavy compliance tasks on small businesses or the liability issues that might arise from inaccurate reporting. Another proposal, conferring a federal blessing upon states' ability to exclude remote sellers from reaching customers within their borders if firms refuse to abide by a destination-sourcing requirement, would in our opinion open the door to unacceptable depredations upon interstate commerce. It would also give license to the same kind of mischief that MFA would unleash.

To conclude, we believe that if the Committee wishes to recommend for the whole House legislation that addresses the role of remote sellers in the sales tax realm, Members should studiously avoid the Marketplace Fairness Act and the concept of strict destination-based sourcing. Rather, lawmakers should embrace origin-based sourcing for its consistency with the seven principles that Chairmen Goodlatte and Bachus have expressed. Origin-based sourcing inarguably puts all retailers on the same tax-collection footing, while not being any more burdensome for a small remote seller than for a "mom and pop" store. It would not create any new or discriminatory tax obligation, and would at least not be more complex to administer or intrusive on individuals' privacy than current sales-tax laws (however much they may be in need of clarification). Furthermore, the vital underpinning of our federal system – state sovereignty within their borders, with Washington's guidance over commerce outside them – would be preserved, as would the absolutely crucial evolution of tax policy through healthy competition.

Once again, I wish to express our members' gratitude for this Committee's willingness to explore the issue of Internet sales taxes outside the troubling confines of MFA. Please feel free to call upon us in your future deliberations over these and other matters that come before your Committee. Thank you for your consideration of these comments.

Sincerely,

Pete Sepp
Executive Vice President

Statement for the Record

Jim Walters
Macco's Floor Covering, President

to the

House Judiciary Committee

March 4, 2014

Chairman Goodlatte, Ranking Member Conyers and Distinguished Members of the Committee, my name is Jim Walters. I thank you for this opportunity to provide this written testimony in support of the Marketplace Fairness Act ("MFA"). The Act is of great importance to me as an owner and operator of a brick and mortar retail business and is crucial to allow me to compete fairly with Internet sellers. It is also important to me as an individual citizen as it relates to the fairness of taxation.

I am President and co-owner of Macco's Floor Covering. The company was started in 1976 with a single store in Green Bay, Wisconsin. I started with the company in 1977, working part time at minimum wage while putting myself through school. I eventually became a co-owner and helped to grow the company to include, as listed in Attachment 1, six retail locations in Wisconsin and one in Florida. The company operates in everything from lower priced do-it-yourself to middle and high-end full service markets, selling carpet, resilient vinyl, ceramic tile, natural stone, area rugs, hardwood and laminate flooring. We currently provide jobs to approximately 110 employees. In addition, we provide work to a large number of local independent contactors that install the flooring Macco's sells.

I submit this written testimony to explain the need for the Marketplace Fairness Act. My testimony is based on personal experience as a local brick and mortar retailer.

I. Unfair Competition by Internet Sellers

My own company embraces the Internet. We have invested in websites for our stores, participate and initiate blogs on new products, use social networking and interact directly with online consumers. We do not seek to inhibit the Internet or online selling: all we seek is to be allowed to compete fairly with our online competitors with regards to the issue of sales tax collection.

The problem is the inability of states like Wisconsin and Florida to enforce fully their existing sales tax laws to include Internet sales. This, in turn, gives the Internet seller an unfair,

and in my humble opinion, an unethical advantage. This is not hypothetical for the flooring industry. Internet sellers routinely advertise "no sales tax" as a low price marketing gimmick to potential consumers. At Macco's, we can and do match Internet prices, but that is not enough. We are then forced to reduce their price further by the equivalent of the sales tax—the very sales tax that we are mandated by law to collect from the consumer.

New flooring in a home can cost thousands of dollars. As result, consumers generally want to see and touch the flooring before purchasing. Just like many other industries, I have seen an increase in Internet sales in the flooring industry. Just in the past few weeks, we had a customer use our design staff and showroom to select an Armstrong hardwood floor. When we presented a quote of nearly $10,000 plus sales tax of $550, the consumer said that a company on the Internet advertised the exact product at a similar price, but touted no sales tax required. We had to lower the price by the tax amount to secure the order in which we had invested many hours of work. With the increased consumer awareness of the internet this sales tax unfairness has become an all too common occurrence. The frustration is not that the Internet is direct competition. We can and do match Internet prices. The frustration lies in the fact the Internet seller has an unfair advantage due to sales tax collection. The Marketplace Fairness Act would simply level the playing field.

Internet sales of flooring are increasing rapidly, especially with the introduction of easy to install floors. Today, a consumer can install a hard surface floor without any glue or nails. It simply "floats" over the existing substrate. Today there are many flooring products that a consumer can buy and install him or herself. This is a testimony to the ingenuity, research, development and forward thinking of our industry manufacturers such as Armstrong, Mohawk, and Shaw Industries. The problem is not consumer access to these products. My own stores sell these very products. Rather, the problem is that Internet sellers are selling them with no sales tax, creating an unfair and unearned advantage over the local brick and mortar store.

The proposed MFA provides a fair solution to this problem. The Act allows, but does not require, a state to have Internet sellers collect the sales tax just like local retailers do. Accordingly, the Act put the decision where it belongs, at the local state level. Sales taxes are set at the state level to provide for local services and needs. These taxes pay for fire and police departments, libraries, parks and a host of other local projects and services. The loss of the sales tax on Internet purchases can only lead to higher taxes on the citizens to support these local needs.

II. House Judiciary Committee Basic Principles

I have addressed below the "Basic Principles on Internet Sales Tax" set forth by the Committee on September 18, 2013.

1. Tax Relief

The MFA does not create a new tax, nor does it require any state to enact any new tax. All it would do is allow states to enforce the sales taxes they already have. It is key to note that it is the consumer who pays the sales tax. The tax is due on all items the consumer purchases whether at a local store or from a remote Internet seller. The problem is there is no practical way

to collect the tax unless the seller collects it at the time of purchase, which has historically been the mandate of brick and mortar retailers. Accordingly, all local retailers are obligated to have internal accounting systems in place to collect the appropriate sales tax and send to their state governments. All the MFA does is allow state to require that the remote Internet sellers also collect sales tax from its customers just like the local brick and mortar stores now do. Accordingly, the MFA does not create a new tax anymore than enforcing existing tax laws creates a new tax. Rather, it simply creates a practical means of collecting the taxes that are already due.

2. Tech Neutrality

As a brick and mortar store owner, I am definitely at a disadvantage to online businesses. In essence, out-of-state Internet sellers have a "no sales tax discount," and that discount is often the difference between the local stores making or losing a sale. The MFA simply puts the brick and mortar store on equal footing with the Internet seller so that all competitors operate under the same taxation rules.

3. No Regulation Without Representation

Sales taxes are the essence of the local tax. They are determined by state and local governments whose officials are subject to answering directly to local residents. These taxes support local services and projects, such as fire and police departments, libraries and parks. The consumer, whether he or she buys locally or from a remote Internet seller, lives in the locations where the tax is due and benefits from the services for which these taxes pay. The Internet seller does not pay them. Rather, all that the MFA would do is authorize states to require Internet sellers to collect the sales tax so that the local consumer, who elected the local officials and who benefits from these taxes, pays his or her fair share.

4. Simplicity

I do not see taxing Internet sales as creating a significant burden on the Internet seller. A company can easily account for, collect, file the monthly paperwork and remit the taxes collected for the different rates using today's computer systems. Internet sellers already have a sophisticated knowledge of computers. The Internet businesses sell online. As a result, they use computer systems that obtain the needed authorization for credit cards, that verify addresses for shipment and that track inventory and the products they ship to consumers. A system to calculate a sales tax based on the customers location takes nothing more than inputting the customer's address. This could not be easier since the Internet seller already loaded the customer's address for delivery at the time of sale. These very same accounting processes have been in place by brick and mortar retailers for many years.

Moreover, the MFA would require a state to meet the standards for simplifying their sales tax rules, provide the Internet seller free software to implement the collection and remittance of the sales taxes that are already due on these sales, and allow Internet and mail order sellers to elect to register with the "one stop" system covering all participating states. Accordingly, it costs nothing, is easy to use and uses the information the Internet seller already collected, such as the consumer's address for delivery.

The MFA would not impose any significant burden on small business. The software is free and uses the very information already collected by the Internet seller to determine the tax that must be collected. The Internet business can also elect to use a centralized one-stop multi-state registration system, further minimizing any burden. The current MFA establishes an unnecessary small business exception for any entity with less than $1 million of Internet or mail order sales. This is far too large of an exemption. A $1 million is approximately the size of the gross sales of the average retail flooring dealer in the United States. There simply is no need for a small business exception and brick and mortar retailers do not enjoy this same exemption.

5. States' Rights

State and local governments determine whether to have a sales tax and the amount of the tax. These taxes support the state and local services and projects, whose official are directly elected by the local community. The MFA does not impose any federal mandate or require a state to implement a sales tax. To the contrary, the Act leaves it to the states and local jurisdictions to decide whether to implement a sales tax, the amount of the tax, if any, and even whether to participate in the MFA and have remote sellers collect the tax. By allowing states to collect sales taxes that are already due, the MFA frees each state to determine how to use the taxes. In my home state of Wisconsin, our Governor, Scott Walker has already suggested using the money to lowering other state taxes.

6. Privacy Rights

As a local retailer, I already collect sales taxes without violating any privacy right of my consumer. Similarly, Internet sellers' collecting sales taxes would create no new privacy concerns.

III. Conclusion

The MFA is needed to ensure fair competition, a cornerstone of American capitalism, and to allow states to effectively collect the taxes that are already due on Internet sales. Without it, local retailers like me will continue to suffer, local jobs will be lost, tax revenue already owed will not be collected and local communities will suffer. The MFA offers a fair solution without imposing unfair burdens on the Internet seller. The Act will simply allow a level playing field for all competitors, whether a brick and mortar store, exclusively an online retailer or a brick and click business.

Attachment 1

Store Locations

Macco's Floor Covering
2035 Larsen Rd.
Green Bay, WI 54303
Wisconsin 8th District: Rep. Reid Ribble

Macco's Floor Covering
680 S. Westland Dr.
Appleton WI 54914
Wisconsin 8th District: Rep. Reid Ribble

Macco's Floor Covering
1919 Hall Ave.
Marinette, WI 54143
Wisconsin 8th District: Rep. Reid Ribble

Macco's Floor Covering
1058 Green Bay Rd.
Sturgeon Bay, WI 54235
Wisconsin 8th District: Rep. Reid Ribble

Macco's Floor Covering
3112 S. Business Dr.
Sheboygan, WI 53081
Wisconsin 6th District: Rep. Tom Petri

Macco's Floor Covering
3111 Schofield Ave.
Schofield, WI 54476
Wisconsin 7th District: Rep. Sean Duffy

Macco-Hadinger LLC
DBA Hadinger Flooring
15091 S. Tamiami Trail
Ft Myers, FL 33908
Florida 19th District: Currently vacant

Statement for the Record

Charles Whitt, Jr.
Whitt Carpet One President

to the

House Judiciary Committee

March 4, 2014

Chairman Goodlatte, Ranking Member Conyers and Distinguished Members of the Committee, my name is Charles Whitt. I thank you for this opportunity to provide this written testimony in support of the Marketplace Fairness Act ("MFA"). The Act is of great importance to me as an owner and operator of a brick and mortar retail business and is crucial to allow me to compete fairly with Internet sellers.

I am the president of Whitt Carpet One in Salem, Virginia, a family owned local brick and mortar store. My family store sells a full range of flooring, including carpet, hardwood, laminate, vinyl and tile. We have 15 employees, plus we hire independent subcontractors to install the flooring sold. Throughout the year, our company affects the livelihood of approximately 40 families in our local community.

I submit this written testimony to explain the need for the Marketplace Fairness Act. My testimony is based on personal experience as a local brick and mortar retailer.

I. Unfair Competition by Internet Sellers

The Internet can be a positive factor in the American economy. It allows consumers to gather preliminary product information, compare the various types of flooring available, and even allow comparative shopping. I have myself embraced the Internet, developing websites for my stores, blogging on new products, advertising and using social networking. Accordingly, I do not want to limit the Internet or online shopping. All I seek is to be allowed to compete fairly with my Internet competitors.

I believe in a free market economy, but also believe that there is no way that the current environment that shields Internet companies and provides them with an unfair advantage—the collection of sales taxes—fits a fair free market economy. Internet sales of flooring are increasing rapidly, especially with the introduction of easily to install floors. Today, a consumer can install a laminate floor without any glue or nails. Similarly, there are self-adhesive laminates, tiles and vinyl that can be installed by simply peeling off the back sheet and laying the floor tile in place. There are even self-stick carpet tiles, making installation of wall-to-wall carpet easier. There are a host of other flooring products that a consumer can buy and install him or herself. The issue is not the availability of these products, but that Internet sellers are selling them with no sales tax, creating an unfair and unearned advantage over the local brick and mortar store

The problem is the inability of states like Virginia to enforce fully their sales tax laws to include Internet sales. The Federal Government's unwillingness to allow Virginia to mandate that all businesses that sell to Virginia residents and businesses be required to collect and remit sales taxes has caused a part of the Virginia statute to become logistically and economically unenforceable. Beginning on July 1, 2013 the State of Virginia raised its general sales & use tax rate from 5% to 5.3%. Obviously this move was to generate needed revenue as most tax increases are. Had Virginia been allowed to mandate sales tax collections from Internet sales companies, maybe the rest of Virginia consumers would not be paying 0.3% higher tax for goods bought inside the state. Moreover, laws that are knowingly unenforceable only serve to further decay the moral and ethical fiber of the American people, while having little or no effect in fulfilling their intended purpose.

If States are given this opportunity to enforce fully their sales tax laws to include Internet sales, the added revenue could go a long way to helping States fulfill their obligation to balance their budgets, while reducing the pressure to sacrifice much needed services. If States could increase their revenues in this equable way, maybe in the future the Federal Government could reduce some of their funding to States, which would help toward balancing the Federal Budget and controlling the deficit.

The proposed Marketplace Fairness Act provides a fair solution to this problem. The Act allows, but does not require, a state to have Internet sellers collect the sales tax just like local retailers do. Accordingly, the Act puts the decision where it belongs, at the local state level. Sales taxes are set at the state level to provide for local services and needs. These taxes pay for fire and police departments, libraries, parks and a host of other local projects and services. The loss of the tax on Internet sales can only lead to higher taxes to support these local needs.

II. House Judiciary Committee Basic Principles

I have addressed below the "Basic Principles on Internet Sales Tax" set forth by the Committee on September 18, 2013.

1. Tax Relief

The consumer owes the sales tax on all items he or she purchases whether at a local store or from a remote Internet seller. The problem is there is no practical way to collect the tax unless the seller collects it at the time of the sale. The local retailer is obligated to collect the tax on all of its sales. All the Marketplace Fairness Act does, and all that I ask of you, is make the remote Internet seller collect sales tax from its customers just like the local brick and mortar stores do now. Accordingly, the MFA does not create a new tax anymore than enforcing existing tax laws creates a new tax. Rather, it simply creates a practical means of collecting the taxes that are already due.

2. Tech Neutrality

Brick and mortar like mine are at a distinct disadvantage and are not on equal footing with online businesses. The out-of-state Internet sellers have a "no sales tax discount." Internet sellers tout this "discount" claiming that "no sales tax" is due on their sales. Local

brick and mortar stores must collect the tax, and that discount is often the difference between the local stores making or losing a sale. The Marketplace Fairness Act will do no more than allow each state to determine whether they will stop this unfair advantage and let a true and fair free market to work in the flooring industry with all competitors operating under the same rules.

3. No Regulation Without Representation

The consumer, not the seller, pays the sales tax. The consumer, whether he or she buys locally or from a remote Internet seller, lives in the locations where the tax is due and benefits from the services for which these taxes pay. All that the Marketplace Fairness Act would do is authorize states to require that Internet sellers collect the sales tax due so that the local consumer simply pays his or her fair share.

4. Simplicity

I do not see taxing Internet sales as creating a significant burden on the Internet seller. With today's computer systems, the company can easily account for, collect, file the monthly paperwork and remit the taxes collected for the different rates. An Internet seller is already savvy with computer systems, using them to verify addresses for shipment, to get authorization for credit cards, and to advertise their product online. A system to correctly calculate a sales tax based on the customer's location takes nothing more than inputting the customer's address, and the Internet seller already inputted this information when it took down the delivery location at the time of sale.

Moreover, the MFA would require a state to meet the standards for simplifying their sales tax rules, provide the Internet seller free software to implement the collection and remittance of the sales taxes that are already due on these sales, and allow Internet and mail order sellers to elect to register with the "one stop" system covering all participating states. Accordingly, it costs nothing, is easy to use and uses the information the Internet seller already collected, such as the consumer's address for delivery.

Compliance is sufficiently simple to allow any small business to comply. The current MFA establishes a small business exception for any entity with less than $1 million of Internet or mail order sales. This is far too large of an exemption. A $1 million is approximately the size of the gross sales of the average retail flooring dealer in the United States. There simply is no need for a small business exception.

5. States' Rights

Sales taxes are the most local of all taxes. They are determined at the state and local level, not by the federal government. These taxes support the state and local services such as the police and fire departments, parks, libraries, local roads and similar local projects and services. The Marketplace Fairness Act does not require a state to implement a sales tax. To the contrary, the Act leaves it to the states and local jurisdictions to decide whether to implement a sales tax, the amount of the tax, if any, what to use the revenues for and even whether to participate the Marketplace Fairness Act and have remote sellers collect the tax.

Marketplace Fairness Act would allow states to collect sales taxes that are already due, so that each state can determine how to use the revenues.

6. Privacy Rights

As a local retailer, I already collect sales taxes without violating any privacy right of my consumer. Internet sellers' collecting sales taxes should similarly not create any new privacy concerns.

III. Conclusion

The MFA is needed to ensure fair competition, a cornerstone of the America capitalism, and to allow states to effectively collect the taxes that are already due on Internet sales. Without it, local retailers like me will continue to suffer, local jobs will be lost, tax revenue already owed will not be collected and local communities will suffer. The MFA offers a fair solution without imposing unfair burdens on the Internet seller. To the contrary, the Act will allow a level playing field for all competitors, whether a brick and mortar store, exclusively an online retailer or a brick and click business.

Statement for the Record

Roger Wilson
Nampa Floors & Interiors

to the

House Judiciary Committee

March 4, 2014

Chairman Goodlatte, Ranking Member Conyers and Distinguished Members of the Committee, my name is Roger Wilson. I thank you for this opportunity to provide this written testimony in support of the Marketplace Fairness Act ("MFA"). The Act is of great importance to me as an owner and operator of a brick and mortar retail business and is crucial to allow me to compete fairly with Internet sellers.

I am the owner of Nampa Floors & Interiors, a locally-owned second generation family business that will celebrate its 60th anniversary this year. The company currently owns and operates three retail locations in Idaho; one in Nampa and two in Boise. We offer a complete selection of carpet, laminates, vinyl, hardwoods, stone and tile flooring. In addition, we sell lighting, granite and marble counter tops, and kitchen, bath and office cabinets. The company provides local jobs to 49 employees as well as work for independent contractors who install the products Nampa Floors & Interiors sells.

I submit this written testimony to explain the need for the Marketplace Fairness Act. My testimony is based on personal experience as a local brick and mortar retailer.

I. Unfair Competition by Internet Sellers

The Internet is a significant innovation that we ourselves have embraced. We have websites for my stores, we blog on new products, we advertise online and we use social networking to promote our business. Far from wanting to inhibit the Internet, we only want a fair marketplace where our Internet competitors operate under the same rules that we brick and mortar stores do,

The problem is the inability to, of states like Idaho, to enforce fully their sales tax laws to include Internet sales. This, in turn, gives the Internet seller an unfair advantage. This is not

hypothetical for the flooring industry. Internet sellers actively advertise no sales tax. Over the past five years the national average profit margin of a brick and mortar flooring retailer was 1.44%. When an Internet seller claims no sales tax, it immediately has a 6% price advantage. The sales tax on large online purchases, such as flooring, can often be a determining factor. It is not often easy to know exactly how many sales are lost to an Internet seller as a result of a "no sales tax" claim. They do, however, know it happens.

Recently, our employees worked with a customer and a builder to design the interior package of an Injury Rehab Clinic. The customer knew the carpet type and yardage needed based on our work. The customer used this information to find the carpet online for less than 10% above our cost. The customer wanted us to match this Internet price. Taking the sales tax into account, matching the price would have resulted in a lose money. As a result, we lost a sale that we devoted many hours to simply because of the unfair "sales tax discount" that the online seller offered.

In another instance, we lost a large order of luxury vinyl tile to an online source. A couple came to the store and wanted to know about luxury vinyl tile. Our employee extensively demonstrated the features of luxury vinyl tile to the consumers. Nampa employees met with the consumer on several occasions in the store, logging in approximately three hours floor time and several hours writing bids and checking availability of specific colors requested. Several weeks later the consumers came in to return the most recent set of samples they checked out. They had found an online dealer selling the same product. The customers mentioned they did not have to pay sales tax, making the cost hundreds of dollars lower than we could offer with the sales tax that we are obligated to collect. This was a sizeable retail job lost to an online source operating free of the requirement to collect sales tax that govern traditional retailers.

Internet sales of flooring are increasing rapidly, especially with the introduction of easy-to install floors. Today, a consumer can install a laminate floor without any glue or nails. For example, Pergo makes a laminate floor that simply snaps together. Similarly, there are self-adhesive laminates, tiles and vinyl that can be installed by simply peeling off the back sheet and laying the floor tile in place. Carpet manufacturers are selling self-stick carpet tiles, making installation of wall-to-wall carpet easier. There are a myriad of other flooring products that a consumer can buy and install him or herself. The problem is not the availability of these products. We promote and sell them, too. The problem lies in the fact that Internet sellers are selling them with no sales tax, creating an unfair and unearned advantage over local brick and mortar stores.

How can free market economy work where individuals are encouraged to invent, expand, succeed and progress under equal opportunities, when in fact the small-to-medium-sized businesses (the ones offering customer service, warranties and true product knowledge) are penalized for operating at physical locations and hiring local employees? Since state cannot alone fix this problem, the only sensible solution is the MFA. The Act leaves it to the states, where it belongs, to determine its sales tax application. The MFA authorizes, but does not require, a state to have Internet sellers collect the sales tax just like local retailers do now. Sales taxes are set at the state level to provide for local services and needs. These taxes pay for fire and police departments, libraries, parks and a host of other local projects and services. The local residents buying online benefit from those services and projects, but do not pay their fair share.

The loss of the sales tax on Internet sales can only lead to higher taxes to support these local needs.

II. House Judiciary Committee Basic Principles

I have addressed below the "Basic Principles on Internet Sales Tax" set forth by the Committee on September 18, 2013.

1. Tax Relief

Requiring Internet sellers to collect the existing sales tax does not create a new tax. The consumer owes the sales the tax on all items he or she purchases, whether at a local store or from a remote Internet seller. The problem is there is no practical way to collect the tax unless the seller collects it at the time of the sale. The local retailer is obligated to collect the tax on all of its sales. All the MFA does is to allow states to require that Internet sellers also collect sales tax from its customers. The MFA simply creates a practical means of collecting taxes that are already due. The Act does not create a new tax anymore than any law that allows for the enforcement of existing tax laws creates a new tax.

2. Tech Neutrality

Internet sellers are selling products with no sales tax, creating an unfair and unearned advantage over local brick and mortar stores. These out-of-state Internet sellers advertise a "no sales tax" discount. Local brick and mortar stores must collect the tax, and that discount is often the difference between the local stores making or losing a sale. The MFA supports the free market economy where everyone has a fair chance to compete under the same rules. Under the current situation, local stores are not on equal footing with their online competitors.

3. No Regulation Without Representation

The party paying the tax, the consumer, lives in the community were he or she elects the local officials who determine whether to have a sales tax, the amount of the tax and how to spend those tax dollars. These taxes are used to support local services and needs, such as fire and police departments, libraries and parks. The consumer, whether he or she buys locally or from a remote Internet seller, lives in the locations where the tax is due and benefits from the services for which these taxes pay. The Internet seller does not pay the sales tax. Rather, all that the MFA would do is authorize states to require Internet sellers to collect the tax so that the local consumer simply pays his or her fair share.

4. Simplicity

The requirement for out-of-state sellers to collect the sales tax does not impose a significant burden. The collection is not complicated with today's computer system. Accordingly, an Internet seller, who is already savvy with computer systems, should have no problems. Internet sellers already use computers to verify addresses for delivery, get authorization for credit cards, and advertise their product online. To calculate the correct sales tax takes nothing more then inputting the customer's address. This could not be easier since the Internet seller already inputs the delivery location at the time of sale.

Moreover, the MFA would require a state to meet the standards for simplifying their sales tax rules, provide the Internet seller free software to implement the collection and remittance of the sales taxes that are already due on these sales, and allow Internet sellers to elect to register with the "one stop" system covering all participating states. Accordingly, it costs nothing, is easy to use and uses the information the Internet seller already collected, the consumer's address.

Compliance is sufficiently simple so a small business exception is not needed. The current MFA establishes a small business exception for any entity with less than $1 million of Internet or mail order sales. This is far too large of an exemption. A $1 million is approximately the size of the gross sales of the average retail flooring dealer in the United States. There simply is no need for a small business exception.

5. States' Rights

It is key to recognize that state and local governments determine whether to have a sales tax, the amount of the tax, and how to speed those funds. These taxes support the state and local services and projects. The MFA does not require a state to implement a sales tax. To the contrary, the Act leaves the states and local jurisdictions to decide whether to implement a sales tax, the amount of the tax, if any, and even whether to participate the MFA and have remote sellers collect the tax. The important factor is that all sales taxes are local and that the very elected officials who decide sales tax issues are directly responsible to their constituents. The MFA does not create a national tax, but simply allows states to enforce the tax fairly to all purchases. If a state's voters do not want sales taxes collected on Internet sales, the state can decide not to take advantage of the authority in the MFA to collect the tax from online sellers.

6. Privacy Rights

There should be no privacy issues. As a local retailer, I already collect sales taxes without violating any privacy right of my consumer. Internet sellers' collecting sales taxes would create no new privacy concerns.

III. Conclusion

The MFA is needed to ensure fair competition, a cornerstone of the America capitalism, and to allow states to effectively collect the taxes that are already due on Internet sales. Without it, local retailers like me will continue to suffer, local jobs will be lost, tax revenue already owed will not be collected and local communities will suffer. The MFA offers a fair solution without imposing unfair burdens on the Internet seller. To the contrary, the Act will allow a level playing field for all competitors, whether a brick and mortar store, exclusively an online retailer or a brick and click business.

Attachment 1

Store Locations

Nampa Floors & Interiors
2121 E Plaza Loop,
Nampa, ID 83687
Idaho 1st District: Rep. Raul Labrador

Nampa Floors & Interiors
1276 S Maple Grove Rd,
Boise, ID 83709
Idaho 1st District: Rep. Raul Labrador

Nampa Floors & Interiors
5874 W State St
Boise, ID 83709
Idaho 2nd District: Rep. Mike Simpson